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Supreme Court of the United States

OCTOBER TERM, 1938

No. 312

JOHN M. TAYLOR, OSCAR A. KENNEDY AND H. RUSSELL HASTINGS, AS THE INDEPENDENT COMMITTEE FOR THE PROTECTION OF THE HOLDERS OF PREFERRED STOCK OF DEEP ROCK OIL CORPORATION,

Petitioners,

vs.

STANDARD GAS AND ELECTRIC COMPANY, REORGANIZATION COMMITTEE OF DEEP ROCK OIL CORPORATION, H. N. GREIS, TRUSTEE OF DEEP ROCK OIL CORPORATION, AND DEEP ROCK OIL CORPORATION,

Respondents.

BRIEF OF PETITIONERS

NOTE: References to the Record are shown as to Volume, by Roman numerals, and as to page, by Arabic numbers, i. e. (II-300), is Volume Two, page 300.

I. OPINIONS OF COURT BELOW

The District Court rendered no opinion in the instant case. The opinions of the Circuit Court of Appeals for the Tenth Circuit are officially reported in 96 Fed. (2) 693-710 and in this Record at I-477-505.

II. JURISDICTION

The decree of the Circuit Court of Appeals was entered on April 27, 1938 (I-505). A petition for rehearing was filed on May 25, 1938, and was denied on June 6, 1938 (I-507-526, 527). This Court granted Certiorari on October 10, 1938, pursuant to petition for Certiorari filed on August 30, 1938. The statutory provision which is believed to sustain the jurisdiction of this Court is Section 240 (a) of the Judicial Code as Amended (28 U. S. C. A., Sec. 347).

III. STATEMENT OF THE CASE

1. Orders Appealed From

Petitioners seek to review certain orders in 77-B Bankruptcy proceedings for the reorganization of Deep Rock Oil Corporation, a Delaware Corporation (hereinafter referred to as "Deep Rock" or "Debtor"). By these orders, the District Court for the Northern District of Oklahoma compromised and allowed in the amount of $5,000,000 an alleged claim of Standard Gas and Electric Company (hereinafter referred to as "Standard") against the Debtor, its wholly controlled subsidiary, and as part of the compromise of this claim, confirmed a plan of reorganization for said Debtor (I-363, 393, 428). By these orders, Standard secured the major portion of the equity in the Debtor's assets at the expense of a five million dollar class of public preferred shareholders of the Debtor, who were thereby practically eliminated.

From these orders, Petitioners, a committee of preferred shareholders of the Debtor, appealed to the United States Circuit Court of Appeals for the Tenth Circuit (I-1-15, 436-

64), which affirmed said orders by a divided court (I-477-505). Circuit Judges Phillips and Williams each wrote an opinion for affirmance (I-477, 499) and Circuit Judge Bratton wrote a dissenting opinion (I-500-505). The primary issues in this case revolve about Petitioners' contentions as to the invalidity of the Standard claim, the impropriety of its compromise, and the unfairness of the allocation of the Debtor's assets under the plan of reorganization.

2. Debtor's Business and Capital Structure

Deep Rock was organized in 1919 by Standard and its affiliated interests through the purchase of a going oil business (II-629, 635-43). Its original name, Shaffer Oil and Refining Company, was subsequently changed to its present name (II-631). Since early 1921, Standard has owned between 95% and 98% of the common stock, being the sole voting stock of Deep Rock (I-260, II-629-31, 688-9). Through the ownership of this stock, Standard has elected all of Deep Rock's Directors and has been in full control of Deep Rock (II-385, 422, 427-8). Standard's officers and directors at all times constituted a majority of Deep Rock's Board of Directors (II-325-56, 427-8, 463). The remaining directors of Deep Rock were operating officers or employes of Deep Rock who had been hired by Standard (II-325-56, 4-5, 9, 36, 41, 63, 70, 422). Standard's top officers including its President, First Vice-President and others, were at all times the top officers of Deep Rock as well (II-325-56, 5, 8, 145, 147, 151).

Standard is one of the largest public utility holding companies of this country. (See *Bonbright and Means, The Holding Company* (1932), pp. 94, 114.) Its securities are listed on the New York Stock Exchange (II-603, 688-9). It carries on no business of its own except as it controls its subsidiary companies (II-7-8). Its published statements

show consolidated balance sheets of itself and its subsidiary companies, in which total assets are listed at over one billion dollars (II-603, 688-9). The only subsidiary included in these consolidated statements that was not engaged in the public utility business was Deep Rock (II-602).

The Debtor went into Federal Equity Receivership on March 2, 1933, under a consent receivership (I-23). In June, 1934, this receivership was transferred into 77-B proceedings and the former receiver was appointed Trustee for the Debtor (I-25).

The Debtor is engaged as an integrated unit in the oil industry, producing, refining and selling gasoline, oil and other petroleum products (I-364, II-735). Its principal place of business is Tulsa, Oklahoma (I-36). It owns and operates 488 producing oil wells, 44 gas wells and a large refining plant (II-735). It owns or controls oil leases covering over 118,000 acres of oil lands located principally in Oklahoma, Kansas, Texas and Arkansas (II-735). It has its own pipe line gathering system totaling over 400 miles, and owns and operates approximately 600 tank cars (II-735-6). In addition, it distributes and sells its gasoline and other oil products through approximately 700 filling stations throughout the Midwest and Southwest territory (II-21, 736).

The capital structure of the Debtor consists of:

(1) *Notes* This is an issue of $10,000,000 of six per cent notes of Deep Rock which matured March 1, 1933, and upon which no interest has been paid since that date (II-722-3). The notes were sold to the public through Standard and its affiliated top-holding company, Byllesby and Company, investment bankers. Except for a few large holders, these notes are widely spread among over

four thousand small holders throughout the country (I-328-9, II-11, 420).

(2) *Preferred Stock* The preferred stock of the Debtor consists of 50,000 shares of non-par stock which is entitled on liquidation to $100 per share, making a total of $5,000,000 for the entire issue. Accumulated dividends of $7 per share per annum, unpaid since 1931, increase the preferred shareholders' right of participation in the Debtor's assets to a total of approximately $7,000,000 (II-114, 613, 631, 722-3, 821). All of the preferred shares with but few exceptions were likewise sold to the public through the same agencies and are held among over 1500 widely scattered shareholders (II-114, 419-21).

(3) *Standard's Common Stock and Claim.* Standard is the owner of practically all of the common stock of the Debtor (I-260, II-688-9). It also asserts a claim as a creditor of the Debtor in the amount of approximately $9,300,000 on the balance of a so-called "open account" between itself and the Debtor (I-23).

3. Standard Claim

The validity and extent of the Standard claim has been the basic problem in the reorganization of the Debtor (II-425). From the inception of the Debtor's receivership, the Standard claim as a creditor has been under attack as invalid in its entirety. Standard filed its claim in the equity receivership and renewed it in the 77-B proceedings (I-23, II-245, 266-276). The Receivers and the Trustee of the Debtor filed objections to the allowance of this claim (II-276-290, I-108-137). By these objections it was urged that the open account charges on which Standard's claim is based are fraudulent and unsustainable and that in any event the entire claim is invalid under the so-called "instru-

mentality" rule of law. Hearing on the claim and the objections thereto was referred by the District Court to a Special Master (I-65). Extensive proofs for both Standard and the Trustee were taken and completed after a full trial lasting many months (II-1-376, 592-681, III-1-127).

All of the witnesses who testified at these hearings were officers, directors or agents of Standard or its affiliates, including the operating officers of the Debtor (II-1, 19, 25, 31, 36, 55, 57, 62, 75, 100, 102, 107, 144, 145, 151, 223, 312-56, 606-8). All of the witnesses were friendly and none of them either expressed or indicated any hostility to Standard (II-377). Many of the salient facts appear by written instruments, books and records and many others were agreed upon in a comprehensive stipulation of facts (II-242-376). *Thus, the entire evidence with reference to the Standard claim was substantially uncontroverted.*

By these uncontroverted proofs it appeared that the open account on which Standard bases its claim covers transactions between Standard and Deep Rock from the latter's inception in 1919 until its receivership in 1933 (I-61-63). The book entries of debits and credits contained in this open account total many thousands of items reflecting thousands of transactions between the two companies throughout this period (II-437, 33-7, III-27-53). These book entries were at all times made under the direction of Standard's own auditing department, which also supervised Deep Rock's auditing department (II-62-65, 69, 188, 49. 606-8, 652-76). This open account shows that during this 14 year period there was charged by Standard against Deep Rock a total of debit entries exceeding $52,000,000, offsetting which are credits for repayments by Deep Rock totaling approximately $43,000,000 leaving a net debit balance of $9,342,642.37, which Standard claims to be owing from the Debtor (I-61-63).

The transactions reflected by this open account range from the expenditure of a few cents to transfers involving millions of dollars at a time (I-61-63, III-27-53). It includes thousands of charges for Deep Rock obligations and expenses paid by Standard directly to third persons (II-42, 57-8, 78-93, 114-15, 172, 179, 184, 195-6, III-27-40, 41-53, 83-7). It also contains huge charges representing an apportionment to Deep Rock of Standard's business expenses, including expenditures for office rentals, salaries, bookkeeping charges, auditing services, stationery, telephone bills and salaries and traveling expenses of various Standard officers (III-27-53). The open account also includes entries for some seventeen millions of dollars of cash advanced by Standard to Deep Rock which from time to time were repaid to the extent shown by the credit entries (I-61-63).

However, by far the largest part of the open account consists of charges arising out of purely inter-company transactions between Standard and Deep Rock (I-61-63). These transactions were, as we shall see, dictated by Standard without any independent voice by Deep Rock's operating officers who were, throughout, subordinates of Standard's top officials. Some $20,000,000 of these charges are under attack in these proceedings by reason of their fraudulent and wrongful nature which, if eliminated from the open account would not only wipe out the entire Standard claim but would leave Standard substantially indebted to Deep Rock (I-335-346). In addition, it is urged that Standard has no right whatsoever to any claim as a creditor of Deep Rock by reason of the applicability of the "instrumentality" rule of law (I-328-30).

A full discussion of the uncontroverted evidence produced at the trial on the merits of the Standard claim appears herein under the Argument portion of this Brief

and further discussion of those facts is therefore omitted at this point. That uncontroverted evidence, as we shall show, discloses that as a matter of fact and law, Standard's claim as a creditor of Deep Rock is invalid in its entirety.

All proofs in the trial on the merits of the Standard claim were closed on February 13, 1935, when both the Trustee and Standard rested their case (II-241-2). *While the question of the validity and extent of the Standard claim was then fully submitted for decision by the Special Master, no decision was rendered either at that time or at any time since, despite the constant urgings of Petitioners for such decision* (I-245, 334, 214).

4. Formation of Respondent Reorganization Committee

Meanwhile, immediately upon inception of the Debtor's receivership, Byllesby and Company, top-holding company controlling Standard, initiated the respondent Reorganization Committee to represent holders of both notes and preferred stock of Deep Rock (II-312, 395, 423-4, 465, 717). This Committee was and is headed by John J. Shinners, as Chairman (II-717, 819). Mr. Shinners is a Vice-President of Byllesby and Company and testified that Byllesby and Company picked the entire personnel of the Reorganization Committee (II-423-4).

A plan of reorganization was first promulgated by the Reorganization Committee in August, 1934, while the hearing on the Standard claim was still in progress (II-819). By January, 1935, before the proofs on the Standard claim had ended, requisite majority consents for approval of this Plan had already been obtained (I-138-42). By this Plan, hereinafter referred to as the First Plan, Deep Rock's preferred shareholders were to be wiped out, and a new $2,500,000 issue of preferred stock

was allocated entirely to Standard (II-823). In addition, Standard was to receive 75% of the new common stock of the reorganized Company, with a little less than 10% of the common stock to be allocated to the preferred shareholders of the Debtor in full satisfaction of their rights (II-823). The Plan provided, however, that the allocation to Standard was predicated on the assumption that Standard would succeed in establishing its claim as a creditor of the Debtor in the amount of at least $5,000,000 (II-824-5). Prior to confirmation of this First Plan, it was therefore necessary for Standard to secure allowance of a $5,000,000 claim.

5. First Compromise Proposal for Allowance of Standard Claim at $5,000,000 Rejected

Instead of awaiting the decision of the Special Master in the completed trial on the merits of the Standard claim, Standard and the other respondents submitted to the District Court a so-called "compromise" proposal to allow the Standard claim at $5,000,000. This compromise proposal, referred to herein as the "first" compromise proposal, was submitted to the District Court on March 8, 1935, about three weeks after completion of the trial on the merits of the Standard claim (I-102-7). The District Court ordered a hearing on the propriety of the acceptance of this first compromise proposal before the same Special Master who had heard the completed proofs on the merits of the Standard claim (I-107).

At the hearing before the Special Master, acceptance of the compromise proposal was recommended and urged by the Trustee of the Debtor, by Standard, and by the Reorganization Committee (II-376-400, 380, 400, I-200). The Taylors, predecessors of petitioners, alone opposed its approval (I-200). The Taylors, John M. Taylor and William H. Taylor, were holders of 550 shares of Deep Rock pre-

ferred stock who, on February 21, 1935, had intervened in the 77-B proceedings (I-99-102). The Taylors had purchased these shares in 1928 on the recommendation of Byllesby and Company at a cost of $48,000 (I-316, II-510). Upon their intervention, they had filed objections in behalf of themselves, as well as all other holders of preferred shares as a class, to the allowance of the Standard claim in any amount whatsoever for the reasons hereinbefore set forth (I-96-99, 335-447). At the close of this hearing on the first compromise proposal, the Special Master recommended its acceptance (I-201-2).

The matter then came on before the District Judge on September 23, 1935, for hearing on the Taylors' Exceptions to the Special Master's Report (I-211, II-400). At the conclusion of this hearing, the District Judge set aside the Special Master's findings, completely rejected this first compromise proposal and ruled that the objections of the Taylors urging the disallowance of the entire Standard claim were "sustained" (I-244-5).

In the course of his opinion rendered in open Court, the District Judge said, in part:

> "The Court: Here is the situation. You cannot get $10,000,000 noteholders and $5,000,000 worth of preferred stockholders, it is hard to get them to concentrate in a unified fight for their interest, whatever it may be. They are scattered all over the country. • • •
>
> Now there is no need to go any further with this argument. I am thoroughly convinced. I have been studying this case, and that is the reason I had it set down for further argument, *my conscience wouldn't let me approve this compromise* from just hearing the arguments. Here is $5,000,000 worth of (preferred) stock outstanding; somebody got that money from the public. Now under this settlement, if I was to approve it, and in approving the plan of reorganization, I would just as well say to the (preferred) stockholders, you

are wiped out; you get a little piece of paper called common stock that I wouldn't give one cent for. * * *

The evidence is overwhelming the Standard ran this company; they officered it; they capitalized it; it is just a child in their hands, and if there ever was a case the law is clear on, it is nothing in the world but an instrumentality, according to the admissions. * * *

Now I am just indicating to you the things I think will be reasonable, and may be it will help you out, but *if you cannot reach a settlement, I will enter an order denying the claim on the ground that the instrumentality rule applies*" (II-406-7). (Our italics.)

Thus, the Honorable District Judge rejected the first compromise proposal on a finding that the Standard claim was invalid in its entirety. Were it not for the rejection of the first compromise proposal at the instance of the Taylors, the first Plan of Reorganization with its complete elimination of the preferred shareholders, would have been adopted (I-244-5, II-399, 406).

6. Second Compromise and Amended Plan Approved

A period of over a year from the time of the rejection of the first compromise proposal then elapsed, during which no action was taken by respondents towards adjudication on the merits of the Standard claim. Notwithstanding the District Judge's finding as to its invalidity, the Standard claim has never been adjudicated on its merits, despite the Taylors' and Petitioners' continued insistence on such an adjudication (I-245, 334, 214).

On November 9, 1936, without even conferring with the Taylors who had been the sole objectors to the first compromise, Standard came in with a so-called new offer of compromise of its claim, herein referred to as the "second" compromise proposal (I-296, II-731-4). *By this second compromise proposal, it was again proposed*

that the Standard claim be allowed at $5,000,000, although exactly such an allowance had already been rejected in the first compromise proposal (I-105-7, II-731-4). At the same time, the respondent Reorganization Committee came in with a proposed Amended Plan of Reorganization which was made by its terms a part of Standard's new compromise proposal (I-276, II-717).

a. Terms of Amended Plan.

Under the Amended Plan, as finally approved by the District Court, the Debtor is to have a new capital structure of $10,000,000 of notes and 520,000 shares of common stock, allocated as follows (II-722):

(1) Noteholders are allocated all of a new $10,000,000 issue of six per cent income debentures in lieu of the present issue in the same principal amount. For interest accumulated to January 1, 1937, in the total amount of $2,300,000, the noteholders are to receive $1,200,000 in cash and 40,000 shares of the new common stock. All interest subsequent to January 1, 1937, is to be paid in cash (I-378).

(2) Preferred Shareholders are completely eliminated from their preferred position and in full satisfaction of their present seven million dollar right of participation in the Debtor's assets, they are allotted 100,000 shares of the new common stock.

(3) Standard receives for its $5,000,000 claim, 380,000 shares of the new common stock. It receives presumably nothing for its ownership of the present common stock of the Debtor.

Thus, Standard is allocated approximately 73% of the new common stock, as against 19% to the preferred shareholders, with the remaining 8% allocated to the noteholders.

b. Petitioners' Objections to Second Compromise and Amended Plan.

This second compromise proposal and Amended Plan was set for hearing before the District Judge on December 12, 1936 (I-288, 299). In the meantime, in July, 1936, the Taylors had caused the formation of the Independent Committee for the Protection of the Holders of Preferred Stock of Deep Rock, Petitioners herein, who thereupon intervened in the case and were substituted as Intervenors in the place of the Taylors (I-311-327, 357-8). At the hearing of December 12, 1936, Petitioners, as representatives of the public holders of 10,295 shares of preferred stock, being over 20% of the entire issue, presented their written objections to the Amended Plan and Second Compromise in behalf of the preferred shareholders as a class (I-33-4, 328-54, 420-24).

The objections of Petitioners to the Amended Plan and Second Compromise were substantially as follows (I-328-54, 420-24):

(1) That the compromise allowance of the Standard claim at $5,000,000 was unwarranted inasmuch as the Standard claim was invalid in its entirety as disclosed by the substantially uncontroverted evidence in the completed trial on the merits of that claim.

(2) That the District Court had already recognized the invalidity of the entire Standard claim at the time of the rejection of the first compromise proposal, and in any event had adjudicated that a compromise allowance of that claim at $5,000,00 was unwarranted.

(3) That the compromise proposal was contrary to the best interests of the preferred shareholders and was unduly favorable to Standard.

(4) That the Plan of Reorganization was based on an unfairly low appraisal of the Debtor's assets, which resulted in an unfair and inequitable discrimination in favor of Standard at the expense of the preferred shareholders, in the allocation of the equity in the Debtor's assets.

(5) That the offer and acceptance of the Plan was in bad faith with the aim of unlawfully enhancing Standard's interests at the expense of the public preferred shareholders.

c. Proofs at Hearing on Second Compromise.

At the hearing of December 12, 1936, Standard and the Reorganization Committee urged acceptance of the Amended Plan and Second Compromise proposal but produced no proofs in justification of the compromise allowance of Standard's claim at $5,000,000. The Chairman of the Reorganization Committee, Mr. John J. Shinners, Vice-President of Byllesby and Company, claimed that the Reorganization Committee knew nothing of and did not concern itself with the propriety or fairness of the compromise proposal (II-446-451). He stated that the Reorganization Committee urged acceptance of the compromise solely in reliance on the recommendation and approval of the Trustee (II-446-451). It appeared moreover that, prior to the hearing, a letter had been sent to the securityholders by the Reorganization Committee urging them to refrain from joining with Petitioners in opposing the compromise proposal (II-682-4). This letter read in part:

> "The Trustee of Deep Rock and his Counsel have approved the new compromise" (II-683).

The Trustee and his Counsel, however, specifically belied both the testimony of Mr. Shinners and the representation made in this letter, when they stated in open Court that they were making:

"no recommendations here on behalf of the Trustee to either accept or reject the compromise" (II-524).

Thus, neither the Reorganization Committee nor the Trustee attempted to justify the fairness or propriety of this compromise allowance of Standard's claim. Standard alone urged the acceptance of this compromise allowance of its claim. However, even Standard offered no testimony whatever on the fairness of such compromise.

The only proofs with reference to the propriety of the compromise allowance were those offered by petitioners in opposition to it. As proof of the invalidity of Standard's claim, petitioners offered in evidence the entire record in the completed trial on the merits of the Standard claim, which was accepted by the District Judge as part of the proofs before him, and is included in this Record on appeal (II-556-7). In addition, petitioners produced other testimony showing the unfairness of the compromise proposal, including a full cross-examination of the Chairman of the Reorganization Committee, supplementing the record on which the District Court had rejected the first compromise proposal (II-419-469, 508-514, 542-555).

Furthermore, the unfairness of the compromise was made particularly apparent by the appraisal which the proponents of the Plan submitted at the same time and which was approved by the District Judge. This appraisal fixed a total valuation of approximately $17,000,000 on the Debtor's assets (I-358-61, 371-2). There being some $12,000,000 owing to the noteholders for principal and interest, there was left only a $5,000,000 equity to be shared by Standard and the preferred shareholders. With Standard being allowed a claim as a creditor for $5,000,00, no equity was left for the preferred shareholders. Thus, the preferred shareholders were as completely eliminated by the compromise

allowance of the Standard claim at $5,000,000 as they would be by the allowance of the entire Standard claim at over $9,000,000. The compromise was thus clearly contrary to the best interests of the preferred shareholders and was beneficial only to Standard.

At the close of this hearing, the District Judge approved the compromise allowance of the Standard claim at $5,000,000, but rendered no opinion, either written or oral, in support of his adjudication (I-393-6). Nor did he make any attempt to explain or reconcile his approval of this compromise in the face of his former rejection of exactly the same compromise amount, and particularly in the face of his own finding that the entire Standard claim was invalid (II-406-7).

d. Proofs at Hearing on Amended Plan.

On the fairness of the Plan as a whole, the only testimony offered by its proponents was that of Mr. Shinners, Vice-President of Byllesby & Company and Chairman of the Reorganization Committee (II-411-19). He admitted that the same Standard officials who were also the top officers of the Debtor, are his superior officers at Byllesby and Company (II-422-3, 433). The extent of his partisanship for Standard was shown throughout his testimony under cross-examination at this hearing (II-419-467, 508-514). At one point he was asked whether he knew that the testimony on the Standard claim showed gross misrepresentations by Standard to Deep Rock's public securityholders. Mr. Shinners characteristically replied:

> "If you are asking me to impeach and try my associates with respect to their integrity, Mr. Honigman, I am not going to do it" (II-462).

On the whole, his testimony disclosed many evasions and contradictions. His entire basis for supporting the fair-

ness of the Plan was his explanation that the Plan was fair provided that Standard had a valid claim for $5,000,000 and provided that the proponents' appraisal of the Debtor's assets was a fair one (II-444-453). At best, his testimony merely begged the basic questions in issue.

Other than the testimony of Mr. Shinners, the only evidence introduced by the proponents in support of the fairness of the Plan was the testimony dealing with the so-called Trustee's appraisal of the Debtor's assets. No dispute is here involved with reference to the fair value of the Debtor's current assets which consist mainly of cash and which total a net amount, over and above current liabilities, of approximately $7,300,000 as of October 31, 1936 (I-361).

With reference to the fixed assets, the valuation of which is in dispute, the proponents of the Plan presented at this hearing a valuation of $9,500,000 (I-358-361). That appraisal was by far the lowest valuation ever submitted for the Debtor's fixed assets. A full discussion of the impropriety and unfairness of that appraisal appears in the Argument portion of this brief. As we will there show, this appraisal, approved by the District Court, was neither fair nor disinterested. Moreover, this appraisal admittedly gave no consideration whatever to the earnings or earning power of the Debtor as a going concern (II-501, 504, 528-9, 566).

The proponents of the Plan justify the practical elimination of preferred shareholders from participation in the assets of the Debtor by claiming that under their appraisal of $17,000,000, there is no equity left for preferred shareholders after providing for some $12,000,000 of principal and interest on the notes and $5,000,000 for the Standard claim. Thus, as we shall show, through the device of an unfairly low appraisal, the rights of the public preferred

shareholders are obliterated. The District Judge accepted this palpably low and unfair appraisal, without any opinion or explanation (I-393) and in the face of his own statement made in open court that this appraisal was "low" by reason of its failure to consider the Debtor's earnings (II-566).

Respondent Reorganization Committee voted in approval of the Amended Plan approximately 83% of the Notes and 58% of the preferred stock of the Debtor (II-579). As we shall hereinafter show, the testimony in the hearing before the District Court further developed that the respondent Reorganization Committee was acting in bad faith and that the largest individual preferred shareholders of the Debtor had joined in acceptance of the Plan for selfish reasons of their own, and were not concerned with the best interests of the preferred shareholders as a class. A full discussion of the unfairness of the offer and acceptance of the Plan appears in the Argument portion of this brief.

e. District Court's Approval of Second Compromise and Amended Plan.

About one week after the conclusion of this hearing, the District Judge, without written or oral opinion, entered orders approving the compromise allowance of the Standard claim at $5,000,000 and confirming the Amended Plan of Reorganization (I-363, 393, 428). Petitioners appealed from these orders to the Tenth Circuit Court of Appeals under both Sections 25 and 24-b of the Bankruptcy Act (I-1-15, 436-64). These appeals were there consolidated (I-17-21).

7. Decision of Circuit Court of Appeals

The Circuit Court of Appeals affirmed the decision of the District Court by a divided Court (I-477-505). Separate opinions for the majority were rendered by Circuit Judges Orie L. Phillips and Robert L. Williams (I-477, 499). A dissenting opinion was rendered by Circuit Judge Sam G. Bratton (I-500-505).

Both majority opinions refused to pass upon the validity of the Standard claim on its merits (I-492, 499). The gist of both majority opinions is that they saw no reason to disturb the discretion of the District Judge in approving the compromise allowance of the Standard claim, and confirming the Plan of Reorganization of which it was a part.

Circuit Judge Bratton, in his dissenting opinion, unequivocally held that the Standard claim as a creditor was invalid in its entirety by reason of the applicability of the Instrumentality Rule of law (I-504). He further held that in view of the invalidity of the Standard claim, the Plan of Reorganization was necessarily unfair and inequitable and the orders of the District Court should be reversed (I-504-5).

IV. SPECIFICATIONS OF ERROR

The District Court erred in its orders of December 22, 1936, and February 3, 1937, and the Circuit Court of Appeals for the Tenth Circuit erred in affirming them, because

1. Under the substantially undisputed facts of the instant case and as a matter of law, Standard was entitled to no claim as a creditor of Deep Rock, by reason of the applicability of the Instrumentality Rule.

2. Under the uncontradicted and overwhelming weight of the evidence, a total of $20,000,000 of specific items of charges included in Standard's account against the Debtor are invalid and unsustainable. (See specific items listed in Record at I-338-345.) If only one-half of these wrongful charges are eliminated, it requires the complete disallowance of the entire Standard claim.

3. The validity of the Standard claim should have been adjudicated on its merits.

4. The compromise was contrary to the best interests of the preferred shareholders of the Debtor and was unwarranted under all of the circumstances of the instant case.

5. The instant compromise was precluded by reason of *res adjudicata* resulting from the District Court's rejection of the first compromise proposal.

6. The compromise proposal was not presented or recommended by the Trustee, nor was there any proof of fairness thereof, contrary to the provisions of Section 27 of the Bankruptcy Act and General Order in Bankruptcy No. 33 (11 U. S. C. A., Secs. 50 and 53).

7. The compromise proposal was a fraudulent device to release Standard from its burden of proving the fairness of the transactions with Deep Rock upon which its claim on

the open account is based, contrary to the rule of law that attaches a presumption of fraud to dealings between common directorates.

8. The compromise was inserted as part of the Plan of Reorganization, contrary to the provisions and intent of the 77-B Act.

9. The Plan was unfair in that it unfairly allocated the major portion of the Debtor's assets to Standard at the expense of the public preferred shareholders of the Debtor.

10. The Plan was unfair in that it was wrongfully predicated on the assumption that Standard has a valid claim as a creditor of Deep Rock in the amount of $5,000,000.

11. The Plan was unfair in that it was wrongfully predicated on the so-called Trustee's Appraisal of the Debtor's fixed assets, which appraisal was unfairly low, was not made by disinterested persons, and failed to take into account the earnings or earning power of the Debtor as a going-concern.

12. The Compromise and Plan were offered and accepted in bad faith by Standard, the Debtor, the Respondent Reorganization Committee, and by the largest individual holders of preferred stock.

13. The District Court and the Circuit Court of Appeals should have refused to approve and confirm the Compromise and Plan and should, instead, have denied the allowance of any claim to Standard by an adjudication on the merits of the Standard claim and should have adjudicated that the Debtor was the owner of all of the assets of the Refining Company, free of any claims on the part of Standard or its nominees.

V. SUMMARY OF ARGUMENT

By the compromise allowance of the Standard claim coupled with confirmation of the Plan of Reorganization for the Debtor, a $5,000,000 class of public preferred stockholders have been deprived of their investment in the Debtor. Standard justifies the practical elimination of the preferred shareholders on the ground that it is a creditor of Deep Rock to the extent of $5,000,000 and that after providing for its claim, there is no equity left for the preferred shareholders under the appraisal submitted by respondents. Petitioners deny that Standard is properly a creditor of Deep Rock in any amount and further deny that the appraisal submitted by respondents is a fair one.

Petitioners urge that the compromise allowance of Standard's claim at $5,000,000 was entirely unwarranted. The completed proofs in the trial on the merits of the Standard claim show that that entire claim is invalid. The proofs in that trial disclose by substantially uncontroverted evidence that Standard was throughout in complete and fraudulent domination of its subsidiary, the Debtor, under circumstances requiring application of the Instrumentality Rule of Law in complete denial of its claim as a creditor. Moreover, these undisputed proofs show that Standard's claim is based on a self-dictated open account balance which contains huge charges arising out of fraudulent and unsustainable inter-company transactions. Upon the elimination of these wrongful charges, there remains no balance owing to Standard on this open account. Whether on the basis of the Instrumentality Rule or because of the unsustainability of the specific items charged into the open account, Standard in fact and law has no valid claim against the Debtor.

If, as we contend, Standard has no valid claim against the Debtor, no compromise allowance of that claim at

$5,000,000 can be justified. Respondents secured the allowance of the Standard claim by the instant compromise in order to evade the consequences of an inquiry into the true merits of that claim. The facts and circumstances under which this compromise was proposed clearly expose it as a faithless attempt to secure for Standard a $5,000,000 claim when, in fact and law, it has no claim whatsoever.

Petitioners furthermore urge that respondents submitted an unfairly low appraisal of the Debtor's assets, which was prepared by prejudiced parties and admittedly gave no consideration to the Debtor's earnings as a going concern. Under a fair appraisal of the Debtor's assets, there would be left a very substantial equity for the preferred shareholders, even assuming that Standard has a valid $5,000,000 claim. Through the device of an unfairly low appraisal, however, the public preferred shareholders are deprived of their rightful participation in the Debtor's assets.

Moreover, the offer and acceptance of the Plan of Reorganization were made and procured in bad faith. The Respondent Reorganization Committee, organized and controlled by the Standard interests, misled the public securityholders into accepting the Plan of Reorganization. Furthermore, the largest individual holders of preferred shares accepted the Plan by reason of special interests of their own not common to the preferred shareholders as a class.

By reason of the foregoing, it is submitted that the orders of the District Court approving the compromise allowance of Standard's claim and confirming the Debtor's Plan of Reorganization should be reversed.

VI. ARGUMENT

A.

STANDARD'S CLAIM SHOULD BE DENIED UNDER THE INSTRUMENTALITY RULE OF LAW

1. The Instrumentality Rule Requires the Denial of a Parent Company's Claim as a Creditor Upon the Receivership or Bankruptcy of Its "Instrumentality" Subsidiary.

Before entering into a discussion of the facts of the instant case calling for the application of the Instrumentality Rule in denial of Standard's claim as a creditor, it is necessary to first consider the principles of law which constitute the so-called Instrumentality Rule.

The Instrumentality Rule is a fairly recent development of the law. This Court was among the first to blaze the trail in the recognition and development of that Rule. The Rule has been stated by this Court to be a broad equitable rule of law, that separate corporate entities of a parent and subsidiary will be disregarded by the courts

> "• • • where stock ownership has been resorted to, not for the purpose of participating in the affairs of a corporation in the normal and usual manner, but for the purpose • • • of controlling a subsidiary company so that it may be used as a mere agency or instrumentality of the owning company. • • • In such a case the courts will not permit themselves to be blinded or deceived by mere forms of law but, regardless of fictions, will deal with the substance of the transaction involved as if the corporate agency did not exist and as the justice of the case may require." (From the opinion of Mr. Justice Clarke in *Chicago, M. & St. P. Ry. v. Minn. Civic Assn.*, 247 U. S. 490, 501, 62 L. Ed. 1229, 1237).

This rule has often been applied by this Court in piercing the forms of separate corporate entities "as the justice of the case may require." Under the decisions of this Court, the parent company has been held liable for the obligations of its "instrumentality" subsidiary on contracts and torts and also as the real offender in statutory violations committed through its "instrumentality" subsidiary.

Davis v. Alexander, 269 U. S. 114, 70 L. Ed. 186 (1925).

McCaskill v. U. S., 216 U. S. 504, 54 L. Ed. 590 (1910).

U. S. v. Lehigh Valley R. Co., 220 U. S. 257, 55 L. Ed. 458 (1911).

U. S. v. Del. L. & W. R. Co., 238 U. S. 516, 59 L. Ed. 1438 (1915).

Hart Steel Co. v. Railroad Sup. Co., 244 U. S. 294, 61 L. Ed. 1148 (1917).

U. S. v. Reading Co., 253 U. S. 26, 64 L. Ed. 760 (1920).

The lead of this Court in the enunciation of this rule has been followed by similar decisions throughout the courts of this country.

American Nat. Bank v. National Wall-Paper Co., 77 Fed. 85 (C. C. A. 8, 1896).

Baltimore & Ohio Tel. Co. v. Interstate Tel. Co., 54 Fed. 50 (C. C. A. 4, 1893).

Bank of U. S. v. Cuthbertson, 67 Fed. (2) 182 (C. C. A. 4, 1933).

Bishop v. United States, 16 Fed. (2) 410 (C. C. A. 8, 1926).

Costan v. Manila Electric Co., 24 Fed. (2) 383 (C. C. A. 2, 1928).

Dillard & Coffin Co. v. Richmond Cotton Oil Co., 140 Tenn. 290, 204 S. W. 758 (1918).

Dunnett v. Arn, 71 Fed. (2) 912 (C. C. A. 10, 1934).

Fourth Nat. Bank v. Portsmouth C. Oil Refn. Corp., 284 Fed. 718 (C. C. A. 5, 1922).

Industrial Research Corp. v. General Motors Corp., 29 Fed. (2) 623 (D. C. Ohio, 1928).

In re Marcella Cotton Mills, 8 Fed. (2) 522 (D. C. Ala., 1925).

Joseph R. Foard Co. v. State of Maryland, 219 Fed. 827 (C. C. A. 4, 1914).

Lucey Mfg. Corp. v. Oil City Iron Works, 15 La. App. 12, 131 So. 57 (1930).

Luckenbach S. S. Co. v. W. R. Grace & Co., 267 Fed. 676 (C. C. A. 4, 1920).

Maloney Tank Mfg. Co. v. Mid-Continent Petroleum Corp., 49 Fed. (2) 146 (C. C. A. 10, 1931).

National Bank of Commerce of Seattle v. Dunn (Washington, 1938) 78 Pac. (2) 535.

Penn. Canal Co. v. Brown, 235 Fed. 669 (C. C. A. 3, 1916).

Spokane Merchants Assn. v. Clere Clothing Co., 84 Wash. 616, 147 Pac. 414 (1915).

Stark Elec. R. Co. v. M'Ginty Contracting Co., 238 Fed. 657 (C. C. A. 6, 1917).

The Willem Van Driel, Sr., 252 Fed. 35 (C. C. A. 4, 1918).

Tower Hill-Connellsville Coke Co. v. Piedmont Coal Co., 64 Fed. (2) 817 (C. C. A. 4, 1933).

Wallace v. Tulsa Yellow Cab & Baggage Co., 178 Okla. 15, 61 Pac. (2) 645 (1936).

Westinghouse Elec. & Mfg. Co. v. Allis Chalmers Co., 176 Fed. 362 (C. C. A. 3, 1910).

See too,

Powell, Parent and Subsidiary Corporations (1931), pp. 1-114.

Latty, Subsidiaries and Affiliated Corporations (1936).

Anderson, Limitations of the Corporate Entity (1931).

Wormser, The Disregard of the Corporate Fiction (1927).

The Instrumentality Rule has likewise been applied to deny the parent company's claim as a creditor upon the receivership or bankruptcy of its "instrumentality" subsidiary.

Albert Richards Co. v. The Mayfair, 287 Mass. 280, 191 N. E. 430 (1934).

Baker Motor Vehicle Co. v. Hunter, 238 Fed. 894 (C. C. A. 2, 1916).

Centmont Corp. v. Marsch, 68 Fed. (2) 460 (C. C. A. 1, 1933).

Clere Clothing Co. v. Union Trust & Sav. Bank, 224 Fed. 363 (C. C. A. 9, 1915).

E. E. Gray Corp. v. Meehan, 54 Fed. (2) 223 (C. C. A. 1, 1931).

Edward Finch Co. v. Robie, 12 Fed. (2) 360 (C. C. A. 8, 1926).

Henry v. Dolley, 99 Fed. (2) 94 (C. C. A. 10, 1938).

In re Burntside Lodge, Inc., 7 Fed. Supp. 785 (D. C. Minn. 1934).

In re Kentucky Wagon Mfg. Co., 71 Fed. (2) 802 (C. C. A. 6, 1934).

In re Otsego Waxed Paper Co., 14 Fed. Supp. 15 (D. C. Mich., 1935).

S. G. V. Co. of Dela. v. S. G. V. Co. of Pa., 264 Pa. 265, 107 Atl. 721 (1919).

Powell, Parent and Subsidiary Corporations (1931), pp. 112-115.

Latty, Subsidiaries and Affiliated Corporations (1936), pp. 142-155.

Anderson, Limitations of the Corporate Entity (1931), Sec. 347.

The basis for the application of the Instrumentality Rule in the denial of a parent company's claim against its dominated subsidiary is succinctly stated in the oft cited case of *S. G. V. Company of Delaware v. S. G. V. Company of Pennsylvania*, 264 Pa. 265, 268, 107 Atl. 721 (1919). Mr. Justice Walling there said:

> "In the establishment and conduct of the business the (Delaware) company furnished about $147,000 for which it took the (Pennsylvania) company's notes on the basis of loans. These financial transactions were made on the orders of the directors of the Delaware company, in which the directors of the Pennsylvania company as such took no part. • • •
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> • • • True, the Pennsylvania corporation continued as a separate entity, notwithstanding the fact that its stock was all held by the Delaware Company (*Point Bridge Co. v. Pittsburgh & West End Co.*, 230 Pa. 289, 79 Atl. 567; *Com. v. Monongahela Bridge Co.*, 216 Pa. 107, 64 Atl. 909, 8 Ann. Cas. 1073; *Monongahela Bridge Co. v. Pittsburgh, etc., Traction Co.*, 196 Pa. 25, 46 Atl. 99, 79 Am. St. Rep. 685, 10 Cyc. 1277); but equity looks at the substance of the transactions, and where one corporation conducts its own business through the instrumentality of another and in its name, the capital invested therein by the former cannot be treated as a loan to the latter as against the rights of third parties. In other words, one who invests money in his own business cannot, in case of failure, shift the loss to innocent parties because of the name under which the business was done or the manner of doing it. • • •
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> • • • 'What it chose to call these supplies of money is of no serious moment. The law pays little heed to the label parties put upon their transactions.' *Brunswick v. Hoover*, 95 Pa. 508, 513 (40 Am. Rep. 674).

Under such circumstances, the controlling corporation cannot share as a creditor in the assets of the insolvent subsidiary company. Any other rule would defeat justice and open the door to fraud. This principal is often applied in bankruptcy cases in the federal courts. See *In re Watertown Paper Co.*, 169 Fed. 252, 255, 94 C. C. A. 528; *Colonial Trust Co. v. Montello Brick Works*, 172 Fed. 310, 312, 97 C. C. A. 144; *Hunter v. Baker Motor Vehicle Co.* (D. C.), 225 Fed. 1006, 1016, 1017; *Brown v. Pennsylvania Canal Co.* (D. C.), 229 Fed. 444, affirmed in *Pennsylvania Canal Co. v. Brown*, 235 Fed. 669, 149 C. C. A. 89; and see, also, *Day v. Postal Telegraph Co.*, 66 Md. 354, 7 Atl. 608." (Italics ours.)

As universally recognized, the Instrumentality Rule is a broad rule of equity. It is used by the courts as an instrument of justice in circumventing the purely legalistic restrictions imposed by the ordinary concepts of the separateness of corporate entities. By that Rule, courts are enabled to pierce through the forms of corporate structure and to accomplish justice in accordance with the substantive relationship of the parties rather than the ostensible forms. Ordinarily, the separateness of corporate entities is maintained and recognized by the law. Where, however, one corporation so fully controls and dominates another for its own ends as to make the latter, in effect, its own agency or instrumentality, the courts have applied the Instrumentality Rule to impose upon the dominating parent company its true position as the owner, principal or real party in interest.

The underlying principle of abuse of corporate control which calls for the application of the Instrumentality Rule has been clearly enunciated by this Court as well as the other courts of this country. The facts and circumstances which require the finding of an instrumentality relationship differ, however, with the facts and circumstances of each particular case. The factual situations under which

the Instrumentality Rule has been applied by the courts generally disclose situations of interlocking officers and directorates, dummy officers, dummy directors, parental financing of the subsidiary, payment of salaries and other expenses of the subsidiary, payment of the subsidiary's obligations directly to third persons, inadequate capitalization of the subsidiary, handling the subsidiary as if it were a department of the parent company, recognition of the subsidiary as part of the parent company's business, disregard of legal formalities in dealing with the subsidiary, servility of the subsidiary's management in dealings with the parent, unfairness or misrepresentations by the parent in dealings with third parties having an interest in the subsidiary, mishandling or misappropriation of the subsidiary's assets for the benefit of the parent. See *Powell, Parent and Subsidiary Corporations* (1931), pp. 7-19; *Latty, Subsidiaries and Affiliated Corporations* (1936), pp. 142-155. As disclosed by the decisions, no particular one of these elements is essential for the finding of the Instrumentality relationship. Nor is it necessary to have any particular combination of these elements. It is only that one or more of these elements in some combination or another have formed the basis for a finding that the Instrumentality relationship exists. In the instant case, we shall show that almost all of these elements evidencing the Instrumentality relationship are to be found from the substantially undisputed facts developed in the trial on the merits of the Standard claim.

We respectfully submit that after a careful examination of the reported decisions, we have been unable to find a single instance where the circumstances under which the Instrumentality Rule was applied showed anything that even approached the gross abuse of the corporate relationship that is disclosed by the Record of the instant case. It is submitted that the undisputed facts of the

instant case, as hereinafter developed, require that the entire Standard claim be denied within the principles of the Instrumentality Rule and that Standard's net advancements, if any, be relegated to the position of a capital investment in the Debtor.

2. The Undisputed Facts Show Complete, Fraudulent and Wrongful Domination by Standard Over Deep Rock Warranting Application of the Instrumentality Rule in Denial of Standard's Claim.

The Standard claim, as we have seen, was fully tried on its merits. The proofs in that trial consisted of the testimony of Standard's own officers, agents and employes, none of whom were in any respect hostile to Standard. The only other proofs consisted of books, records and written instruments, as well as a comprehensive stipulation of facts. Thus, the evidence with reference to the Standard claim was substantially of an uncontroverted nature. An appreciation of the legal effect of these proofs requires, however, a consideration of the facts thus developed.

a. Standard's absolute control of Debtor shows instrumentality relationship.

The very nature of the open account upon which Standard bases its claim and the transactions reflected therein disclose the instrumentality relationship between Standard and Deep Rock. To understand the nature of this open account and the transactions reflected therein, it is necessary to understand that Standard's business was that of a public utility holding company which through stock ownership controlled its numerous subsidiaries (II-7-8, 603, 688-689). In order to procure the maximum emoluments of its control, Standard used many intermediate corporations such as the Byllesby Engineering and Management Com-

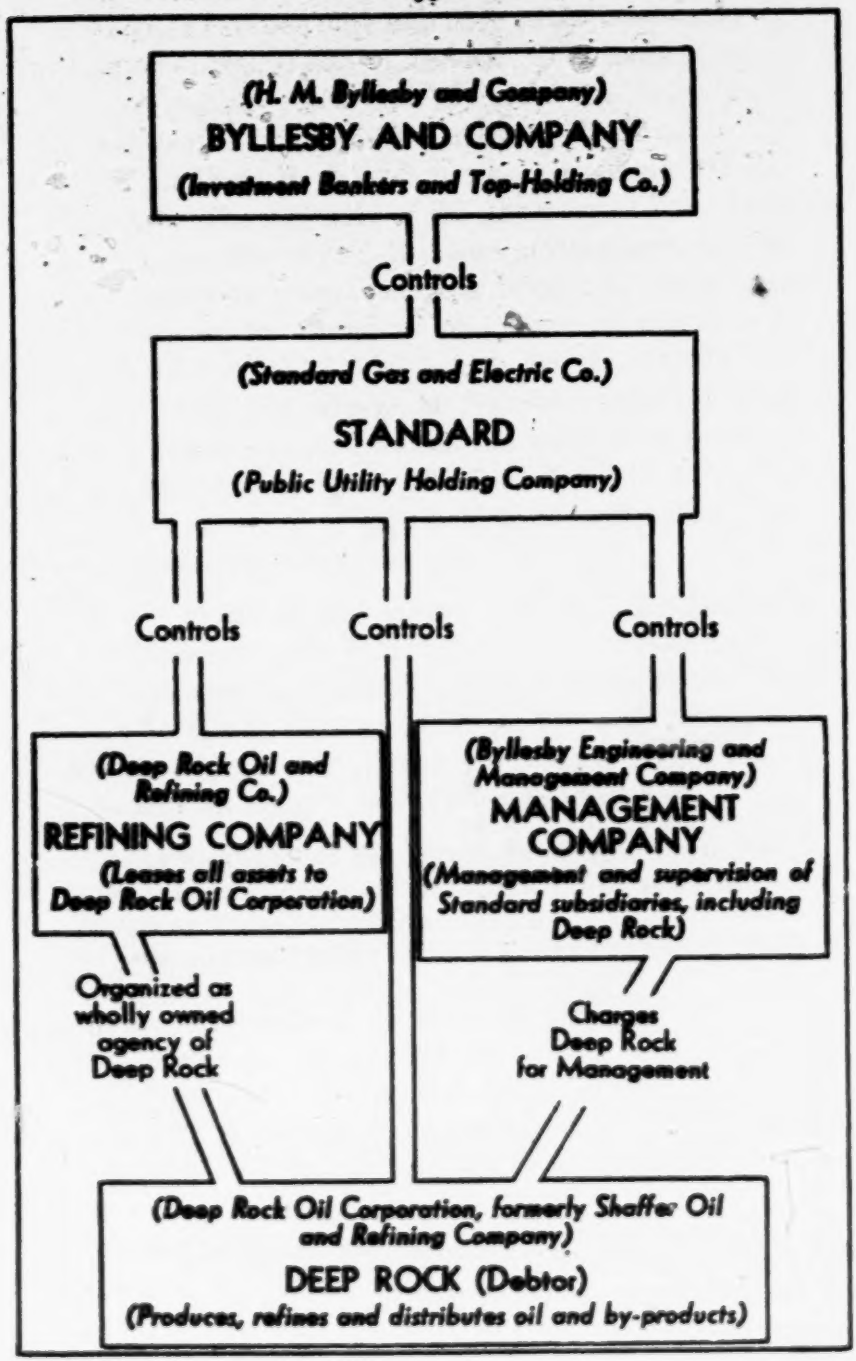
pany, hereinafter referred to as the "Management Company." This company was a wholly owned subsidiary of Standard which ostensibly rendered engineering services and operating advice to the various Standard subsidiaries (II-3, 7-8). Actually, however, the services rendered by the Management Company were as a rule negligible and in the case of Deep Rock, as we shall see, were entirely non-existent. The Management Company, as will hereinafter appear, was primarily a vehicle which Standard employed to mulct its subsidiaries, including Deep Rock.

Standard itself was controlled by the investment banking house, Byllesby and Company, the top holding company of this public utility pyramid (II-2-3). Byllesby and Company, through ownership of the majority of Standard's voting stock controlled with a comparatively small investment, all of Standard's billion dollar public utility empire which had been built up by the investments of public securityholders (II-2-3, 603). The relationship between Byllesby and Company, Standard, the Management Company, and the Debtor was such that they shared the same offices and the same men were at the same time the top-officers of each of these companies (II-8, 55, 312-59, 422, 433-4).

The interrelationship between these companies is shown in graphic form in Chart 1, prepared by us, which appears on the next page. The major portion of the charges included in Standard's open account are inter-company charges made between the companies shown in Chart 1. These charges, as will hereinafter appear, are, for the most part, fraudulent and unsustainable and were imposed on Deep Rock through Standard's complete domination and control. Before considering the actual items of wrongful charges contained in this open account, it is necessary to understand generally the method and extent of Standard's control and domination over the Debtor.

CHART 1

Intercorporate Relationships of Deep Rock, Standard and Affiliates



Standard incorporated the Debtor in 1919 and since early 1921, has owned between 95% and 98% of the common stock of the Debtor (I-260, II-635-41, 688-9). This common stock was the sole voting stock and Standard has been alone during that period in its control of Deep Rock and in the designation of Deep Rock's officers and directors (II-385, 427-8, 629-31). The majority of the directors of Deep Rock were at all times officers and directors of Standard, and the remaining directors were operating officers of Deep Rock who were chosen by Standard and were subordinate to Standard's officers (II-325-56, 4-5, 9, 36, 41, 63, 70, 422, 427-8, 463). The top officers of Standard received their sole salary from Standard but at the same time acted as the top officers of Deep Rock (II-325-56, 5, 8, 145, 147, 151). Thus, there was complete interlocking of both officers and directors of the two companies.

All of the meetings and minute books of the Debtor's Board of Directors were held in the offices of Standard at Chicago, although the Debtor's principal place of business was at Tulsa (II-13, 37, 43, 162, 164-5, 178, 228, 240). Mr. O'Brien (President of Standard, Deep Rock, Byllesby and Company and the Management Company) testified:

> "The meetings of the Directors of the (Deep Rock) were held in Chicago, in my office, in the same office I occupy as President of the Standard. All of the meetings were so held in my office so far as I know" (II-13).

At those meetings, almost all of the directors present were directors or officers of Standard and only on rare occasions were there present a few of the operating officials of the Debtor (II-331-8, 608-629). Inasmuch as at all times the same persons were the top officers of both Standard and Deep Rock, the operating officers of Deep Rock were at all times subordinates of the Standard officials present (II-312-359).

Moreover, Deep Rock's chief operating officers were hired directly by Standard (II-4, 9, 63, 70, 36, 41). With reference to the hiring of John L. Gray, Deep Rock's Vice-President and General Manager, the President of Standard testified:

> "As president of Standard I contracted with Gray as to the salary he was to receive as (vice) president (of Deep Rock)" (II-9).

The uncontroverted evidence and written admissions herein, further disclose that many of the most important transactions of the Debtor throughout the period of its existence, were handled directly by Standard without even the formality of approval by the Deep Rock Board and often without even written agreements (II-42, 28, 30, 78-93, 98, 144-51, 161-2, 172-3, 184-5, 195-6, 244-5, III-27-53). Many of these instances will be later pointed out in our discussion of the specific items of wrongful charges contained in the open account.

The nature and extent of Standard's domination of Deep Rock's business is attested to by Standard's own officers. Its President, Mr. O'Brien, says in this regard:

> "And further I want to say that no important moneys were spent (by Deep Rock) or items approved without the approval of this Chicago office, and that means myself and Mr. Graf (First Vice-President of Standard) principally * * *" (II-6).

He further testified that he was consulted on practically all phases of Deep Rock's business (II-5-6). With reference to the work of Mr. Majewski, Vice-President and Sales Manager of Deep Rock, Mr. O'Brien tells us:

> "Mr. Majewski consulted with me frequently about the affairs of the company. He did not take any affirmative action in any matter of importance without first consulting with me" (II-9).

Mr. Majewski, himself, tells us about an operating committee of Deep Rock composed of its active operating heads, who submitted suggestions:

> "* * * to Mr. O'Brien and his associates for approval or rejection. * * * It took the ultimate approval here, though, of Mr. O'Brien and his associates before any policy was changed" (II-24).

Mr. Graf, First Vice-President of Standard, likewise testified to meetings held in Chicago monthly and sometimes oftener, "concerning operating, financing and marketing conditions" of Deep Rock (II-26). Mr. Cummins, a Standard director and also for two years President of Deep Rock, likewise testified to Standard's active participation in Deep Rock's affairs:

> "I am familiar with the extent to which the officers of the Standard participated in the affairs of Deep Rock.
>
> Q. How frequently, if at all, were there conferences held between the officers of (Deep Rock) and those of Standard? A. I would say that there were general conferences at least once or twice a week. Aside from that, there was hardly a day on which I was not in touch with some member, particularly with the fiscal end of Standard" (II-33).

Mr. Lynch, Chairman of the Standard Finance Committee, testified that the Standard organization kept in "daily touch with all of the affairs of Deep Rock as they affected the financial and accounting department" (II-62). He further explained that his contact with Deep Rock affairs was "what I would term daily conferences" (II-63). Mr. Riddle, an operating Vice-President and Director of Deep Rock, testified in the same regard, as follows:

> "I don't know of any transaction that (Deep Rock) entered into without first consulting Mr. O'Brien and Mr. Graf of the Standard in Chicago * * *" (II-233).

Many officials of Standard were also dummy officials of the Debtor although they were neither under salary nor allegiance to the Debtor (II-144-151). These dummy officials signed for the Debtor notes for millions of dollars payable to Standard, and contracts with Standard involving many millions of dollars which form the basis for Standard's claim on the open account (II-118-22, 144-51, 179-80, 181-197, 201, III-6-16). These same dummy officials likewise signed Deep Rock's checks drawn on Deep Rock's bank accounts, payable to Standard and its affiliates (II-42, 114-15, 171-173, III-1-5, 17-18). The first knowledge Deep Rock would have of the drawing of these checks on its own bank account was by memoranda to that effect in interdepartmental form, sent by Standard or its affiliates to Deep Rock's office at Tulsa (II-79, 171-3, 184-5, 652, III-19-22).

These dummy officials testified that they did not know why the contracts, notes and checks were signed or what their purpose was or whether there was any authorization therefor by the Deep Rock Board of Directors (II-144-151). They testified that they signed for Deep Rock whatever instruments their superiors at Standard directed them to sign (II-144-151).

Typical of the evidence in this regard is the following testimony of one of the Standard officers who signed a $4,250,000 note payable to Standard in his capacity as a dummy officer of Deep Rock:

> "Q. Do you have any recollection of that transaction? A. No, sir.
>
> Q. Do you know what the consideration for that note was? A. No, sir.
>
> Q. Do you know what was done with the $4,250,000? A. No, sir.
>
> Q. Do you know whether or not (Deep Rock) received that sum of money from the Standard Gas and Electric Company? A. No, sir.

Q. Did you know at that time? A. I don't remember now.

Q. By whose direction or authority did you sign the name of (Deep Rock) to that $4,250,000 note? A. I don't recall that now" (II-149).

At a further point in his examination, this dummy official admitted that in the signing of this note as well as many other Deep Rock notes payable to Standard, he was acting solely upon instructions from his superior officers at Standard (II-150-151). Other dummy officials of Deep Rock were not put on the stand when Standard's counsel conceded that their testimony as to the circumstances under which they signed Deep Rock notes, checks and contracts in transactions with Standard would be to the same effect (II-151).

Standard's departmental operation of the Debtor is further evidenced by the thousands of bills and expense items incurred by Deep Rock but which Standard paid directly to third persons, merely charging Deep Rock's open account (II-42, 57-8, 61, 78-93, 114-15, 172-179, 184, 195-6, III-27-40, 41-53, 83-7). Such payments range from a few cents to huge sums, totalling millions of dollars. They cover such widely varying expense items as corporation qualifying fees, revenue stamps on securities, registrar's and transfer agent's fees and expenses, auditing services, insurance premiums, legal services, services of tax experts, materials purchased, oil purchased, safe deposit box rentals, fees for statutory representation service, income taxes, rent, stationery, telephone, telegraph, traveling expenses, directors fees, furniture and fixtures, postage, light, printing, advertising, office equipment, and hundreds of other items too numerous to mention (III-27-53). In addition, Standard paid directly to public securityholders millions of dollars in interest and principal on Deep Rock notes as well as dividends on Deep Rock preferred stock, and

charged Deep Rock therefor through the medium of the open account (I-61, II-59, 78-80, 83, 661-76). A Standard officer explains that:

> "The Deep Rock did not pay anything, but the Standard Gas and Electric Company paid the public and charged (Deep Rock) with the amount of the dividends * * *" (II-80).

Standard's direct control of the Debtor is further evidenced by the fact that the entire proceeds of both a $7,500,000 and $10,000,000 Deep Rock note issue, sold to the public by Standard's affiliate and top-holding company, H. M. Byllesby and Company, was pocketed directly by Standard (I-63, II-60-61, 97). Standard merely credited the Debtor's open account with the proceeds so taken after deducting heavy underwriting charges (I-63, II-60-61, 97).

Standard handled all of the numerous financing of the Debtor, directly supervised the Deep Rock's accounting department, issued orders and made charges on inter-office memorandum forms, and for practical purposes operated the Debtor as a department of its own business (II-5-6, 9, 24, 26, 33, 37, 62, 69, 86, 233, 240, 380, 606-8, 652-76, 689, III-6-15, 19-22, 26, 64-87).

Standard itself considered Deep Rock as a department of its own business (II-4, 5, 7, 10, 31). The Standard officials constantly referred to Deep Rock in their testimony and published documents as being a part of the so-called "Standard System" or "Byllesby Group" (II-31, 62, 63, 87, 100-101, 156, 398). Standard's President, in referring to the acquisition of Deep Rock, testified:

> "So we got into the oil business that way" (II-4).

At a further point, he referred to services rendered by Standard for "all of our properties, whether oil or public

utility" (II-7). Deep Rock's assets and liabilities were moreover included in Standard's published reports as part of its "Consolidated Balance Sheet" (II-592-606). Deep Rock earnings were likewise included as part of Standard's "Consolidated Earning Statement" (II-592-606). Standard, moreover, included Deep Rock's operations as part of its Consolidated Income Tax Returns (II-205-6). In its published Reports, Standard furthermore lists Deep Rock in tables headed "Operated Companies of Standard Gas and Electric Company" (II-592-606). *Thus the uncontroverted evidence discloses beyond question that Standard was in complete control of the Debtor, directly participated in the operation of the Debtor's business, and handled and acknowledged the Debtor as a department of its own business.*

b. Deep Rock's financial dependence on Standard shows instrumentality relationship.

The uncontroverted testimony further disclosed that the Debtor was undercapitalized by Standard in the first instance; that it was in dire need of money throughout the entire period of its existence; and that it was at all times kept in absolute dependence upon Standard for financial aid (I-146, 260, II-7, 16, 26, 30, 33, 35, 37, 41, 42, 73, 224, 229, 293, 405-6, 652-676, 677).

At the time of its organization, Deep Rock was launched with a $200,000 investment in its common stock by Standard and its affiliates by which they secured full control of a $20,000,000 investment in preferred stock and bonds sold to the public (II-613-19, 635-41, 11, 69-70). Deep Rock's initial cash requirements for the purchase and operation of its oil business called for far more cash than was provided for by its initial capitalization (II-613-19, 635-41, 11, 69-70). Accordingly, from the outset it was necessary for it to borrow huge sums which were raised by the public sale of bonds and notes on which, of course, Standard and its affiliates

received heavy underwriting fees (I-63, II-613-19, 635-41, 69-70).

Despite the large public investment at its inception and by subsequent refinancings, Deep Rock was continually kept dependent upon Standard for financial assistance, even for the cash needed for its daily operations (II-652-676). Mr. O'Brien, President of Standard and Deep Rock, frankly admits Deep Rock's utter financial dependence on Standard when he states:

> "Financing of (Deep Rock) was necessary from the date of its purchase up to the time its operations terminated. It was almost a continuous process, as a matter of fact, furnishing money for it. A large part of this service was rendered by Standard, and some of it by H. M. Byllesby & Company" (II-7). * * *
>
> Q. I believe you said during your original examination, which the reporter probably did not take note of, that (Deep Rock) was about two feet in front of the wolf all the time. Is that the statement you made? A. That is the statement I made, yes. I didn't say all the time. I said a good part of the time.
>
> Q. A good part of the time. A. Yes, and if it wasn't for the Standard standing behind it, it would have been in receivership long ago.
>
> Q. A good part of that time, from the time it was started until the receiver was appointed? A. Exactly" (II-16).

Mr. Graf, First Vice-President of Standard, likewise testified:

> "It would have been impossible for (Deep Rock) in its financial condition during the majority of the time from 1919 to 1933, to continue in business without the financial support of Standard" (II-26).

Moreover, Deep Rock's financial dependence resulted not only from the inadequacy of its original capital structure, but was maintained throughout by Standard's whole-

sale looting of Deep Rock's funds, the story of which we are about to consider. Deep Rock's utter financial dependence upon Standard inevitably subjected the Debtor and its officers to complete subserviency in their dealings with Standard. By reason of such dependence, Deep Rock was throughout kept in the position of a mere puppet or instrumentality of Standard.

c. Standard's claim is based on fraudulent inter-company transactions which show instrumentality relationship.

(1) Instrumentality relationship shown by Standard's fraudulent imposition of Refining Company transactions.

Deep Rock's subserviency to Standard was nowhere more evident than in the course of the so-called Refining Company transactions. By these transactions, Standard by its own fiat fraudulently divested Deep Rock of assets upon which Deep Rock had spent over $4,000,000 in acquisition, and in addition, foisted upon Deep Rock over $5,000,000 of fraudulent charges, which are included in Standard's claim on the open account (I-62, II-94-5, 130-3).

The uncontroverted testimony in this regard discloses that in February 1923, Deep Rock purchased certain oil properties known as the "Bradstreet Properties", which it continued to own and develop at its own cost and expense of over $2,200,000 (II-34-6, 44-6, 128-9, 176-7, 194-5, 227). Deep Rock operated these properties in the same manner as its other oil producing properties, without accounting to anyone for income therefrom and expending all sums necessary for operation thereof without charge to any one (II-35-6, 45, 72, 226-7).

In addition, Deep Rock constructed in 1922 a cracking plant as a necessary adjunct to its refinery in the pro-

duction of its gasoline products (II-19-24, 26, 108-9, 218-22). This cracking plant was constructed on the refinery property of Deep Rock and in fact and appearance was an integral part of its refinery (II-108-9, 218-22, 226-7, III-148). It was operated by Deep Rock in the same manner as the remainder of the refinery (II-51, 108-9, 218-22). Its operation was entirely by employes of Deep Rock with all income therefrom handled in the same manner as the income from the remainder of Deep Rock's refinery and all expenses therefor paid by Deep Rock (II-51, 108-9, 218-22). In the construction of this cracking plant and improvements thereto, over $1,800,000 was expended by the Debtor (II-176-7).

The title to the Bradstreet properties and the cracking plant was nominally held by individual trustees for Deep Rock Oil and Refining Company (herein referred to as the "Refining Company"), a purely inactive dummy corporation, all of whose stock was owned by Deep Rock (I-113, II-36, 105-6, 191-2, 198, 294). After three years of operation of these properties by Deep Rock as its own, the stock of the Refining Company was suddenly transferred to Standard solely upon directions of the General Auditor of Standard to his subordinates at Deep Rock (II-48-50, 128, 188, 606-8) with provisions made for crediting Deep Rock's open account with the latter's cost of acquisition up to that date (II-48-50, 128).

Mr. Francisco, Secretary and Treasurer of Deep Rock, acknowledged that the transfer of this stock to Standard was made entirely "on the authority of this letter (dated December 22, 1925) from Mr. Braheney (General Auditor of Standard)" (II-49). He admits, moreover, that there was no authority for the transfer from the Deep Rock Board (II-49). Mr. Kerr, Deep Rock's Auditor, likewise affirms that the transfer of this Refining Company stock

from Deep Rock to Standard was made entirely on the authority of the aforementioned letter from Standard's General Auditor. He testified:

> "I made the entry on the Deep Rock's books showing its (Standard's) purchase of 8,325 shares of Refining Company stock • • • under the authority and direction of Mr. Braheney's letter addressed under date of December 22, 1925" (II-188).

At the same time, a five year lease of these properties from the Refining Company to Deep Rock was drawn by Standard officials and signed at Chicago by Standard officials in their capacity as dummy officials of Deep Rock (I-134-5, II-52, 148, 167, 230, 308, 606-8). *By this lease, Deep Rock became the lessee of the very properties which it had purchased, paid for and operated as its own throughout the three year period since their acquisition.* Neither of the two dummy officials who signed this lease in behalf of Deep Rock was under salary to Deep Rock and the only one of these officials who testified, stated that he knew nothing of this lease agreement nor why it was signed, except as it was common for him to sign Deep Rock instruments at the direction of his superior officers at Standard (II-148-151). His testimony in part was:

> "Q. Do you recall attesting, as Assistant Secretary of (Deep Rock), an agreement between (the Refining Company) and (Deep Rock), dated October 1, 1925, and marked Receivers' Exhibit 'Jay'? A. I do not recall it. I may have attested it.
>
> Q. I hand you this instrument, and ask you to state whether or not that photostatic copy, which is Receiver's Exhibit 'Jay,' shows your signature on there, as attesting the execution by (Deep Rock)? A. It does.
>
> Q. Do you recall anything about that transaction? A. No, sir.
>
> Q. Do you know by whose direction you attested that execution by (Deep Rock)? A. No, sir" (II-148).

This immensely important lease, so executed by Standard's employes in their capacity as dummy officers of Deep Rock was, on March 19, 1926, for the first time sent to Tulsa from Standard's office in Chicago with instructions from the Standard Auditor that it should be signed under date of October 1, 1925, by two of the operating officers of Deep Rock in their capacity as dummy officers of the Refining Company (II-52). *It is admitted by Stipulation of Standard herein that neither this lease nor its renewal of October 1, 1930, was ever "submitted to or approved or authorized by any meeting of the Board of Directors of Deep Rock or the Refining Company"* (II-244). We thus find this highly important lease being executed by dummy officers of both Deep Rock and the Refining Company solely under instructions from Standard, and without even the formality of approval by Deep Rock's Board.

By this lease, Deep Rock leased from the Refining Company, at a rental of $600,000 per year, the very assets which Deep Rock had owned and operated for over three years (I-134-5). The rentals paid under this lease, and interest charges thereon, totaled over $5,000,000 (I-62, II-131-3). Deep Rock paid these, not to the Refining Company, but directly to Standard and these rental charges are included in the open account on which Standard bases its claim (I-62, II-94-5, 152-3). In addition, Standard by its own fiat charged Deep Rock a total of $190,000 for Federal income taxes on Standard's profits from these rentals on the wholly unsustainable assumption that that was another Deep Rock obligation under this lease (II-81-2). Through the medium of this sham lease, Standard obtained for itself over $5,000,000 of Deep Rock's funds.

Moreover, even if it were proper to compel Deep Rock to become the lessee of its own properties, the rentals charged under this lease were grossly exorbitant. The

excessiveness of the rental charges is shown by the record of the operations of the properties covered by the lease (III-23-4). During the period from the inception of the lease to the time of receivership, Deep Rock suffered a net loss in excess of $1,600,000 through the operation of these properties (II-23-4). In addition to this loss, Deep Rock spent over $2,000,000 for improvements and additions to these properties while operating under this lease which, under the terms of the lease, Standard claims as its own (II-176-7, 17, I-134-5). Furthermore, in the first 14 months that these properties were operated by the Receiver there was a net operating loss, even before rentals, of $136,229.30 (II-651).

The utter indefensibility of these rental charges is even admitted by Mr. Shinners, Chairman of the Reorganization Committee and Vice-President of Byllesby and Company:

> "Q. Now then don't you think that the terms of the lease were onerous so far as Deep Rock was concerned? A. I think they were excessive" (II-431).

Despite Deep Rock's tremendous losses during the five year term of this lease, the lease was renewed at its expiration in 1930 for another five years on the same terms and through the medium of the same dummy officials (I-136-7, II-229-30, 244, 429-32, III-23-4). Asked if he protested to the signing of this lease or its renewal, one of the chief operating officers of Deep Rock who was also a director, admitted his utter subserviency to Standard's domination, when he said:

> "I would not have been in position to protest" (II-230).

It is further admitted by Standard that, although two-thirds of the rental charged under this lease was attribu-

table to the leasing of the cracking plant to Deep Rock, the written instrument itself completely omitted any mention or description of the cracking plant (II-244, III-23-4). It is unimaginable that under any circumstances but the most reckless disregard of the subsidiary's separate corporate existence, could a lease of the significance of the instant one be executed with a complete omission of two-thirds of the property being leased.

Despite the execution of the Refining Company leases, Deep Rock continued to operate the so-called Refining Company properties as its own. All additions and new purchases of oil properties even when made in the name of the Refining Company were handled by Deep Rock's employes and paid for entirely with Deep Rock's funds (II-105-6, 194). Since the making of the lease, Deep Rock spent over $2,000,000 of its own money in acquiring such new properties and additions which Standard now claims to be its own as sole owner of the Refining Company (II-176-7, 17, I-134-5). Furthermore, the *ad valorem* tax records on the so-called Refining Company properties continued to be in the name of Deep Rock as owner (II-200). So, too, the insurance policies covering these properties were throughout in the name of Deep Rock (II-202-3).

In the keeping of the depreciation and depletion records, Deep Rock likewise included the so-called Refining Company properties among its own, as shown by the undisputed testimony of Deep Rock's Auditor that:

> "no separate provision was made for depreciation, depletion or retirement losses sustained on the assets of the Refining Company" (II-216).

When it is borne in mind that the entire bookkeeping system was, as we have seen, under the direct domination and control of the Standard Auditing Department, these entries

are significant in their proof that basically the so-called Refining Company assets were throughout known and considered to be the assets of Deep Rock.

The undisputed proofs show that the Refining Company at no time had any independent existence of its own. It never had a bank account, nor did it have any office, active officers, or paid employes (II-105-6, 194). It was entirely an inactive dummy corporation which Standard took over from Deep Rock and used as a vehicle in extorting huge sums from Deep Rock for its own private gain. By these Refining Company transactions, Standard stole from the Debtor assets on which the Debtor has spent over $4,000,000 of its own funds (II-176-7), leased them back to the Debtor, the owner of the assets, and by the lease and its renewal, foisted on Deep Rock about $5,500,000 of fraudulent rental, income taxes and interest charges which are part of the open account on which Standard's claim is based (I-62, II-81-2, 131-33). It is submitted that under the uncontroverted proofs, these fraudulent charges should be eliminated from the open account and the so-called Refining Company properties should be adjudged as belonging to Deep Rock, without any legal right thereto by Standard or the dummy Refining Company.

Bently v. Zebna Oil Co., 76 Okla. 117, 184 S. W. 131 (1919).

Commerce Trust Company v. Woodbury, 77 Fed. (2) 478 (C. C. A. 8, 1935).

Hamilton Ridge Lumber Corp. v. Wilson, 25 Fed. (2) 592 (C. C. A. 4, 1928).

Heim v. Jobes, 14 Fed. (2) 29 (C. C. A. 8, 1926).

Pacific Amer. Gasoline Co. v. Miller (Tex. Civ. App. 1934), 76 S. W. (2) 833.

Veeser v. Robinson Hotel Company, 275 Mich. 133, 266 N. W. 54 (1936).

Walker v. S. W. Mines Development Co. (Ariz. 1938), 81 Pac. (2) 90.

The completely fraudulent nature of these Refining Company transactions is attested to by the Trustee of the Debtor, when he charged that these leases were:

> "nothing more nor less in effect than leases from Deep Rock, as the lessor, to itself, as lessee, but as such operated and were intended by Standard to operate as mere conduits through which Deep Rock's money and income should be diverted to Standard and withdrawn from the Deep Rock's profits to the great injury of the Deep Rock, its preferred stockholders and creditors * * * (These leases) were fraudulent devices contrived by Standard in order to enrich itself to the great injury of the Deep Rock and its stockholders and creditors; that both of said leases should be adjudged unconscionable, fraudulent, and as such, null and void" (I-121). (See also II-391.)

These Refining Company transactions were thoroughly condemned in the dissenting opinion of Circuit Judge Bratton (I-504). Moreover, they were likewise recognized in the majority opinion of Circuit Judge Phillips as transactions in which "Standard exercised its control to the benefit of Standard and to the detriment of Deep Rock" (I-482).

This unanimous version of the fraudulent nature of the Refining Company transactions is of utmost significance, particularly in view of the fact that these were not merely isolated or insignificant instances of Standard's abuse of its control over the Debtor. On the contrary, these transactions involved many millions of dollars and were an aggregate of a series of machinations by Standard which commenced in 1922 and continued throughout the remaining period of the Debtor's existence. *The unanimous finding by the Circuit Court of Appeals of the wrongfulness of the Refining Company transactions is, we submit, an irrefutable adjudication that in its operation of the Debtor, Standard grossly and fraudulently abused its power of control.* It is submitted that this finding of fact calls as a

matter of law for the application of the Instrumentality Rule, as recognized by this Court and by the weight of authority, in denial of Standard's entire claim as a creditor of Deep Rock.

(2) Instrumentality relationship shown by Standard's fraudulent imposition of management fees.

The uncontroverted testimony further disclosed that over $1,200,000 of the Standard claim against Deep Rock is based upon charges by Standard's wholly owned subsidiary, Byllesby Engineering and Management Corporation, herein referred to as the "Management Company", for supervision and management of the Debtor, by the same officials who, at the same time, were also the top officers of Standard and the Debtor (I-62, II-3, 7-8, 28-9, 55, 101, 239, 433-4). The Management Company was formed by Standard in 1919, ostensibly for the purpose of performing engineering and supervisory services for the public utility subsidiaries which Standard operated (II-3, 7-8). Its officers were at all times the same top officers as those of Standard, Byllesby and Company, and Deep Rock (II-8, 433-4, 312-56). It maintained its offices at Chicago in the same offices with Byllesby and Company and Standard (II-3). The sole assets which it used in its operations were a library, desks, maps and draftsmen's tools (II-8). The Management Company has, at all times, been owned in its entirety by Standard and in the fourteen year period of its existence all of its dividends, totaling approximately $24,000,000, were paid directly to Standard, in addition to its payment of all salaries of Standard's officers and employes (II-3, 8, 359).

The purpose of the Management Company is thus described by the Attorney for the Trustee after listening to all of the proofs on the Standard claim:

> "This Management Corporation, that is the same thing Congress has had in this Holding Company bill. • • • Just like all these other public utilities were doing, the purpose is to make a fictitious overhead charge on public utilities in order to maintain their rates. Now this Management Corporation, the Standard owned all of its stock, said so in its annual reports. It received from that company over $23,000,000 in dividends, and (the Management Corporation) never had any assets except pencils and drawing tools • • •" (II-405).

The charges made by the Management Company against Deep Rock for supervision fees ranged between $100,000 to $200,000 per year for services which this Record discloses were never rendered or agreed upon. *It is admitted by stipulation of Standard:*

> *"That there was never submitted to any meeting of the Deep Rock's Board of Directors, or approved by Deep Rock's Board of Directors, any contract whereby it obligated itself to pay the Engineering and Management Corporation fees or charges for management or finance services, or any kind of services"* (II-244).

Standard's counsel, moreover, conceded that as to the charging of these Management fees:

> "There was no contract, written or verbal" (II-28).

Mr. Graf, Standard and Management Company's First Vice-President, admitted that the Management Company's supervision fees were fixed entirely by the Management Company, when he testified:

> "Q. Who fixed the amount of the charges or fees charged to (Deep Rock) for services rendered by the Management Corporation? A. The Directors of the Management Corporation" (II-28).

This was further borne out by Mr. Riddle, Deep Rock Vice-President and Director, when he testified:

"I was never consulted by the Management Corporation with reference to supervision charges made by them. I don't know of any basis upon which charges were made from time to time by that company for management and supervision" (II-239).

Just how these charges were arrived at appears to have been very uncertain. Mr. O'Brien, who was President of the Management Company, Byllesby and Company, Standard and Deep Rock, admitted that he didn't know how the charges were arrived at. He testified:

"I don't know of my own personal knowledge how the amount of charges that were made for these managerial fees by the Byllesby Engineering and Management Company were arrived at * * *" (II-7).

Mr. Graf, Standard and Management Company's First Vice-President, likewise affirms the general haziness of the method of fixing these charges. He testified:

"The charges which were made against (Deep Rock) were based on no rule of thumb" (II-25).

Mr. O'Brien, President of all of these companies, who, as we have seen, didn't know how the Management Company's charges were arrived at, asserted however that those charges "were not adequate for the amount of work we did" (II-7). He could not recall, however, a single employe or official of the Management Company who did any actual work on Deep Rock properties (II-10).

Standard attempts to justify these Management Company charges on the basis that they were for supervising Deep Rock's business operations. Mr. Graf, First Vice-President of Standard and the Management Company, tells us:

"I was a vice-president and director of the Management Corporation. The services rendered by that

> Company to the properties purchased from Shaffer and subsequently operated under the name of the Deep Rock Oil Corporation, or Shaffer Oil and Refining Company were generally of consultative conferences with the officers and employees of (Deep Rock), the approval of all contracts which they proposed to enter into, the development of policy, both from a construction and a merchandising standpoint" (II-25).

The evidence is undisputed, however, that no one in the Management Company knew anything about the oil business (II-4, 14-15, 27). As Mr. O'Brien, President of these companies, testified:

> "We knew nothing about the oil business at that time" (II-4).

The fact is that by admission of Standard, Deep Rock's oil business was actually handled by its operating officers who were well experienced in the oil business and were being paid large salaries by Deep Rock (I-146, II-8-9, 22, 33, 63, 107-8, 223-4).

Standard attempts the further basis for justification of these supervision fees on the ground of the fiscal advice rendered to Deep Rock (II-29, 40-41). To charge for such advice by persons who were at the same time the directors of Deep Rock is an attempt to levy huge charges for services ordinarily rendered by directors of a company in discussing the financial affairs of their company. Such charges are unwarranted in fact and unsustainable as a matter of law.

> *Eshleman v. Keenan* (Dela. Ch. 1936), 187 Atl. 25.
> *McKey v. Swenson,* 232 Mich. 505, 205 N. W. 583 (1925).

Moreover, when financial services were actually performed, such services were specifically charged for. When-

ever Deep Rock issued or refinanced its securities, tremendous underwriting, discount fees, and fees for extension services were charged by these same individuals in their capacity as officers of Byllesby & Company or Standard and now form a substantial part of the open account on which Standard's claim is based (I-63, II-60-1, 74-5, 97, III-15, 15A).

Insofar as any other services rendered by the Management Company to Deep Rock are concerned, the testimony discloses that they were all purely insubstantial fiscal services for which admittedly no substantial charge could be made (II-56, 59). Moreover, in addition to the supervision fees of $1,200,000, the Management Company charged Deep Rock some $67,000 for proportionate parts of the salaries of certain Management Company's officers as well as additional charges for proportions of the Management Company's expenses for items such as rental, telephone and the like (I-62, II-101, III-27-40). These charges to Deep Rock were an arbitrary proportion of the salaries of certain Standard and Management Company officials, presumably for the same services as are covered by the charge for supervision fees (II-101, III-27-40). Why the supervision fees were charged in addition to these charges is nowhere explained.

A consideration of this uncontroverted testimony thus discloses that there can be no conceivable justification for the charges by the Management Company of over $1,200,000 for supervision fees, which Standard imposed upon Deep Rock. *It was admitted by the Chairman of the Reorganization Committee, a Vice-President of Byllesby and Company, that these charges were made for services that were never rendered and were unwarranted in their entirety* (II-433-4). These Management Company charges were likewise characterized by the Attorney for the Trustee as a "fraud" and as "wholly unjustified", after the close of

the proofs on the Standard claim (II-391). To the making of these and other fraudulent charges, the Record does not disclose a single instance of complaint by any of Deep Rock's operating officers.

We thus have here a situation where over $1,200,000 of charges were imposed by Standard through the agency of the Management Company for services that were never rendered and for which there was no agreement, either written or verbal, or even the formal attributes of submission to the Deep Rock Board. Such charges, so rendered, can only be characterized as "fraudulent." The imposition of such charges without complaint by any of the operating officers of Deep Rock, is indisputable evidence of the complete and fraudulent domination by Standard over the Debtor, its "instrumentality" subsidiary. Such facts, under the decisions of the courts, have inevitably called for the application of the Instrumentality Rule of law.

(3) Instrumentality relationship shown by wrongful dividend withdrawals.

Standard paid to itself about $4,500,000 in dividends from Deep Rock during the period of Deep Rock's corporate existence, of which all but $980,000 appears in the open account upon which Standard bases its claim (I-61, II-88-9). The uncontroverted facts disclose that at the time these dividends were paid, Deep Rock had no surplus or profits warranting their payment. The books of Deep Rock, kept under Standard's management, show profits practically throughout the period of its existence (II-649-50). These book profits were used as the basis for declaration of dividends. *It is undisputed however, that at the same time Deep Rock's books and published statements were disclosing substantial earnings, its Federal Income Tax Reports filed for it by Standard as part of*

the latter's Consolidated Federal Income Tax Return, showed tremendous losses (III-90-3, II-205-6).

In this connection, we have prepared a comparative chart which appears on the next page as Chart 2. As Chart 2 discloses, the Federal Income Tax Returns show that Deep Rock, prior to receivership, lost money in every year commencing from 1922, with the exception of the years 1925 and 1926. While the Deep Rock books and published reports show net earnings of over $10,000,000 from 1919 to the time of receivership, the income tax returns show, during the same period, a net loss of over $9,000,000 (Chart 2 and III-90-93).

Even if there had been sufficient net earnings to warrant dividend payments, it could not have been proper to declare these dividends in view of Deep Rock's constant shortage of funds. Its cash shortage was so acute, we have seen, that Deep Rock was deemed in danger of receivership practically throughout the entire period of its existence (II-16). No company having an independent management of its own would submit to the paying out of dividends under such circumstances. For Standard however, the withdrawal of these dividends was merely ordinary procedure in the course of its looting of the Debtor.

The record of the directors present at the time of declaration of Deep Rock's dividends shows that there were never less than a majority of Standard officers and directors and at times all of them were Standard officers and directors (II-608-613, 620-22, 324-331). The few directors present who were not Standard directors or officers were, as we have seen, subordinate operating officers of Deep Rock whose voice in the management of the Deep Rock affairs was purely subordinate and subservient to that of the Standard high command.

In the withdrawal of these dividends, as in the handling of the other Deep Rock affairs, Standard used Deep Rock as an instrumentality for its own ends and without regard to the best interests of Deep Rock or its public security-holders.

(4) Instrumentality relationship shown by Standard's wrongful imposition of illegal compound interest and discount charges.

The Standard claim includes a total of interest and discount charges charged against Deep Rock of over $6,000,000 made up, as follows (I-61-63):

Interest on Open Account Balances....	$4,819,222.07
Interest on Notes Receivable.....	184,087.93
Interest on Five Year 6% Note.....	331,500.00
Discount on $10,000,000 Note Issue....	604,849.20
Discount on $100,500 Bonds.....	19,858.80
Discount on $7,500,000 1926 Note Issue	226,250.00
Discount on $4,250,000 Note.....	170,000.00
Discount on $1,057,300 Note.....	92,672.69
Total of Interest and Discount Charges	$6,448,440.69

The open account charge of $4,819,222.07 is for interest on the open account balances at the rate of 7% per annum compounded monthly on the average daily balances in this open account (I-62, II-86, 106). Interest was computed each month and added to the open account so that the following month, the balance on which Deep Rock paid interest to Standard also included all prior interest charges (II-86). As Mr. Knourek, Standard's Auditor, admitted: "That would be compounding it" (II-86).

The testimony is undisputed that the entire matter of interest and discount charges throughout this period was covered by no written agreement between Deep Rock and Standard and was never submitted to the Deep Rock

CHART 2

A COMPARISON OF THE EARNINGS OF DEEP ROCK AS SHOWN ON ITS BOOKS AND ITS EARNINGS AS SHOWN ON THE INCOME TAX RETURNS FILED FOR IT BY STANDARD

Year	Earnings as shown on books of Deep Rock	Earnings as shown on Income Tax Returns of Deep Rock
1932	$ 95,426.45 (Loss)	$2,692,355.04 (Loss)
1931	146,215.42 (Loss)	3,513,403.82 (Loss)
1930	350,000.00	3,113,662.02 (Loss)
1929	1,365,437.50	944,944.74 (Loss)
1928	1,398,500.00	351,637.51 (Loss)
1927	980,000.00	1,094,569.81 (Loss)
1926	2,801,021.49	1,725,703.59
1925	1,461,911.70	1,159,838.68
1924	77,990.74	605,040.27 (Loss)
1923	25,416.44	2,132,808.77 (Loss)
1922	484,478.04	222,785.07 (Loss)
1921	425,385.89	441,984.59
1920	858,521.53	931,718.36
1919	696,034.81	778,209.93
Total	$10,683,056.27	Total $9,633,751.90 (Loss)

[Data is taken from III-90-93]

Board (II-86-7, 161-2). These interest and discount charges were imposed on Deep Rock without any voice on the part of Deep Rock's operating officers, and were charged into this open account entirely at Standard's dictation (II-86-7, 161-2, I-61-3). The subserviency of Deep Rock's operating officers to the making of such charges, is evidenced by the fact that throughout this Record there does not appear a single instance of complaint on their part to any act by Standard.

Aside from their exorbitance, the basic impropriety of these interest and discount charges is that they arose entirely out of the fraudulent and unsustainable charges contained in the open account. If it had not been for the fraudulent Refining Company transactions, the Management Company's illegal and unsustainable supervision fees, illegally declared dividends and the many other items of wrongful charges contained in the open account, there would have been no net debit balance owing to Standard. On the contrary, as we shall see, the open account would have shown Standard indebted to Deep Rock. In such event, not only would there be no interest owing to Standard but if anything, there would be interest owing from Standard to Deep Rock.

The further impropriety of these interest and discount charges is that at best they arose out of Standard's failure to supply an ample capital structure for the operation of the Debtor's business, thereby necessitating borrowings that would not otherwise have been required. As the organizer of Deep Rock, and its owner, it was Standard's duty to supply ample capital for the establishment and operation of Deep Rock's business. In charging interest to Deep Rock in the magnitude and degree exhibited in this Record, Standard was making huge profits from its own failure to perform its legal duty to launch

its subsidiary with an adequate capital structure. As a result of this failure, Deep Rock, in the fourteen years of its existence, paid out for interest charges a total of over $15,000,000 (II-650).

Furthermore, compound interest charges at these rates are clearly illegal under the laws of Illinois which control.

U. S. Mortgage Co. v. Sperry, 138 U. S. 312, 340, 342, 34 L. Ed. 969 (1891).
Barker v. International Bank, 80 Ill. 96 (1875).
Leonard v. Villars, 23 Ill. 377 (1860).
Union Natl. Bank of Chicago v. L. N. A. & C. Ry. Co., 145 Ill. 208, 226, 34 N. E. 135 (1893).

Moreover, under the circumstances of the instant case, the interlocking relationship between Standard and Deep Rock was such that Standard cannot maintain these self-imposed exactions when called to account by the Debtor or its public securityholders.

Higgins v. Lansingh, 154 Ill. 301, 369, 40 N. E. 362 (1895).

It may be said in favor of the ordinary usurer that he is dealing with one whom he didn't invite or force to come to him. Even that may not be said for Standard. Deep Rock never had the privilege of choosing the lender or the terms of the loan. Standard by its own wrongs made the borrowings necessary. Standard, by its own fiat, fixed the charges for interest and discount. Of Standard's open account charges, over $6,000,000 is accounted for by these extortionate and illegal interest and discount charges so imposed (I-61-3). The record of such conduct must, if anything can, require the piercing of the veil of separate corporate existence upon which Standard bases its claim as a creditor of Deep Rock.

(5) Instrumentality relationship shown by Standard's imposition of other wrongful charges.

In addition to those hereinbefore discussed, there are many other wrongful and unsustainable charges included in the open account that is the basis for Standard's claim against Deep Rock which arose out of Standard's abuse of its control over Deep Rock. A consideration of some of these items appears at a later point herein. Such additional wrongful charges are, however, only cumulative in their evidence of Standard's mishandling of the Debtor. On the whole, we submit, that there can be no doubt that Standard used the Debtor as an instrumentality for the attainment of its own selfish ends without any semblance of regard for the best interests of the Debtor or its securityholders. Throughout the history of the Debtor, Standard mulcted its assets and earnings to the point where, although Deep Rock had tremendous gross earnings, the net results of its operations showed huge losses (II-649, III-93). The true situation of Standard's handling of the Debtor is well characterized by the Attorney for the Trustee, when, after the close of the proofs on the Standard claim, he stated before the District Judge:

> "Now there isn't any doubt that the Standard has manhandled this Deep Rock. As Lord Brougham once said: 'It was the proud boast of Augustus that he found a Rome of brick and left it of marble.' The Standard found the Deep Rock an unsophisticated country maiden and left it a harlot. *There isn't any doubt but what the Standard has absolutely manhandled the Deep Rock* (II-403). • • •
>
> • • • this Deep Rock Company made one hundred and ninety-two million and some odd dollars in thirteen years, and its (book) net profits was a little over ten million. Now that on its face shows that it has been manhandled. Talk about a corporation making one hundred ninety-two million plus in ten years and having only ten million dollars plus in net profits. That on its face shows it has been run in a harum scarum way" (II-405-406). (Italics ours.)

d. Instrumentality relationship shown by Standard's recognition of its open account as a capital investment.

Although Standard now urges that it is a creditor of Deep Rock by virtue of this open account, the fact is that, prior to Debtor's receivership, Standard itself treated this open account as merely a part of its capital investment in Deep Rock. Standard's entire treatment of the open account and the unusual nature of the transactions reflected therein bore none of the ordinary attributes of a debtor-creditor relationship.

It is admitted, for instance, that Deep Rock never entered into any agreement for the repayment of these open account balances, nor was any time of repayment even discussed (II-65, 241). The fact is that Standard distinctly recognized these open account balances as part of its capital investment in Deep Rock when, in 1928, it cancelled approximately $11,000,000 of open account balances and $9,000,000 of preferred stock, for which it took additional common stock of Deep Rock, although at the time it already owned practically all of the Debtor's common stock and hence was not increasing its ownership in the Debtor's assets (II-623-5, 273-5, 68-9, I-59-60).

Mr. Lynch, Chairman of the Standard Finance Committee, explains that the reason for Standard's 1928 cancellation of its immense open account claim and its preferred stock position was a matter "of fair dealing to the preferred shareholders" (II-69). If it was "fair dealing" for Standard to take common stock for the Standard open account in 1928 when Deep Rock was presumably solvent and not in bankruptcy, then "fair dealing to the preferred shareholders" now too requires that Standard recognize its true position to be that of the owner of the common stock equity and not a creditor prior in rights to the preferred shareholders.

e. Standard's fraudulent manipulation of Deep Rock's securities is a further warrant for the application of the Instrumentality Rule.

The uncontroverted evidence further discloses that the notes and preferred stock of the Debtor were sold to the public by Standard and its top-holding company, Byllesby and Company (II-11, 114, 420). Byllesby & Company acted as both principal and agent in its dealings with the public in the sale and purchase of these Deep Rock securities (II-421, 511). From the inception of Deep Rock, Standard and Byllesby and Company maintained a controlled market for these securities and uncontradicted evidence points to fraudulent manipulation of the prices (II-421, 508-11, 642).

Thus, in March 1931, John M. Taylor, one of the petitioners herein, found it impossible to get any information as to the Debtor's 1930 earnings or balance sheet, although he was a substantial holder of Deep Rock preferred stock (II-509-11). He pleaded in vain in his letter to Byllesby and Company that:

> "You have given me nothing by which I can even approximate what the Company (Deep Rock) is doing under today's conditions" (II-510).

He pointed out, too:

> "We bought this security entirely upon the recommendation of Byllesby & Company, and we should look to you to secure this information for us" (II-510).

Mr. Taylor's concern was apparently not without foundation, as disclosed by the letter which about two weeks later was sent by Mr. O'Brien, President of Standard, Byllesby and Company and Deep Rock, by which Deep Rock's stockholders were told for the first time of the cessation of dividends on the preferred stock (III-131).

Thus, at the time when cessation of preferred stock dividends was imminent and the intent of so doing was doubtless known to the Standard and Byllesby high command, they kept to themselves all information of Deep Rock's true condition, even in the face of urgent requests on the part of a substantial stockholder who had made his investment in reliance on their recommendation. Just how Byllesby and Company was using its undisclosed information can well be imagined when we consider that during this period they were admittedly having "market transactions in notes and the preferred stock of Deep Rock as principal and as agents" (II-511).

Just how far the Byllesby stock manipulations went, is further evidenced by their dealings with petitioner Taylor. A little over a month after the occurrence of the above mentioned interchange of correspondence, Mr. Taylor saw a quotation for Deep Rock preferred stock in the Wall Street Journal at 50 bid and 60 asked. He wrote Byllesby and Company that he was interested in selling his stock at that price range (II-509). In reply, he was told that

> "the newspapers quote was in error. We can offer stock of the Deep Rock Oil Company at $35 per share" (II-508-9).

The inference that this newspaper quotation was an "inspired" error needs little imagination, in view of the history we have seen of the Byllesby dealings.

The evidence further discloses that in selling Deep Rock's securities to the public, representations as to the valuations of the Debtor's assets showed amounts that were far in excess of the true valuations and were four times the valuation now claimed by Standard in the appraisal of these assets in the instant case (II-297-301, III-103-120, 125). The undisputed testimony further dis-

closes that in the sale of these securities representations were made as to tremendous earnings by the Debtor at a time when its Federal income tax reports were disclosing heavy losses (II-254-62, 297-301, 593-605, III-103-114, 90-93).

Typical of Standard's glowing description of Deep Rock's situation is the statement in one of the Annual Reports published by Standard for distribution to the public securityholders of itself and subsidiaries:

> "Notwithstanding the exceptional depression affecting the oil industry during the latter half of the year 1923, Shaffer Oil & Refining Company (Deep Rock) had net operating earnings for the year (1923) of $1,175,600.04, which was in excess of all its interest requirements. The company is a well equipped and complete unit, and is in a favorable position to share in the prosperity of the oil industry indicated by the general improvement which has already taken place" (II-593).

At the same time as that report was published to the public securityholders of Deep Rock, the Federal Income Tax Reports were showing a net loss for that year's operations of $2,132,808.77 (III-93). *Similar gross misrepresentations to Deep Rock's securityholders were made by Standard throughout the entire period of Deep Rock's existence* (II-592-606, III-115, 117, 119, 93).

Further uncontroverted evidence discloses that the prospectuses prepared and circulated by Standard, upon which Deep Rock notes were sold to the public by Standard and Byllesby and Company, both in 1926 and 1928, set forth that the cracking plant was owned by Deep Rock, although Standard, as a part of its claim herein, maintains now that the cracking plant was at that time owned by itself, as sole owner of the Refining Company (II-258, 297).

We submit that under the undisputed evidence, there is no room for doubt that throughout the entire history of Deep Rock, Deep Rock's securityholders were preyed upon by Standard, not only by its fraudulent looting of Deep Rock's assets but further by its fraudulent manipulations in the sale and marketing of Deep Rock's securities. In the interests of justice, Standard should not now be permitted to hide behind the cloak of separate corporate entity to establish itself as a creditor of Deep Rock at the expense of the public preferred shareholders.

3. Conclusion—Instrumentality Rule Should Be Applied in Denial of Standard's Claim.

We have thus far examined the uncontroverted facts developed in the trial on the merits of the Standard claim. We have seen that Standard had complete control over the Debtor and its management; that it ran the Debtor's affairs to suit its own ends and without any regard for the interests of the Debtor or the latter's public securityholders; that the operating officers of the Debtor were at all times completely subservient to Standard's top-officers who, at the same time, were also the top-officers of the Debtor; that through dummy officials and by direct intervention, Standard dictated, without restraint, the many fraudulent transactions which form the basis of its claim as a creditor of the Debtor; that Standard misled the Debtor's securityholders through misrepresentations and market manipulations of the Debtor's securities; that Standard exercised all the attributes of a sole owner of the Debtor's assets, yet upon bankruptcy of the Debtor, it seeks to share as a creditor rather than as an owner of those assets. We submit that in no case where the Instrumentality Rule has been applied have there been as many elements showing an instrumentality relationship as appear under the undisputed facts in the instant case. We

submit that within the principles laid down by this Court, the interests of justice require the denial of Standard's claim to share as a creditor of the Debtor at the expense of the public securityholders whose rights have throughout been flaunted.

B.

STANDARD'S CLAIM SHOULD BE DENIED BECAUSE AN ELIMINATION OF THE FRAUDULENT AND UNSUSTAINABLE CHARGES FROM ITS ACCOUNT WILL EXTINGUISH ITS ENTIRE CLAIM

We have hereinbefore urged that Standard's claim as a creditor of Deep Rock should be denied through application of the Instrumentality Rule of Law. It is our further position that aside from the applicability of that principle, there is an additional alternative ground for rejection of Standard's claim.

The open account upon which Standard's claim is based contains huge charges which, we have seen, were fraudulently imposed upon Deep Rock. The total of these charges, as will hereinafter appear, approximates $20,000,000. If only one-half of these are eliminated from the debit charges in this open account, it will leave no net debit balance and thereby eliminate Standard's entire claim.

In considering the validity of the specific items of charges included in the open account it is essential to note that all of the dealings upon which Standard's claim against Deep Rock is based are admittedly dealings between interlocking directors and officers (II-324-56). *This Court, as well as the decided weight of authority, has established the rule that such transactions are presumptively fraudulent.*

Corsicanna Nat. Bk. v. Johnson, 251 U. S. 68, 64 L. Ed. 141 (1919).

Geddes v. Anaconda Copper Min. Co., 254 U. S. 590, 65 L. Ed. 425 (1921).

Western Distributing Co. v. Pub. Serv. Comm., 285 U. S. 119, 76 L. Ed. 655 (1932).

Allied Chem. Dye Corp. v. Steel & Tube Co., 14 Dela. Ch. 1, 120 Atl. 486 (1923).

Farmers Loan & Trust Co. v. N. Y. & M. R. Co., 150 N. Y. 410, 44 N. E. 1043 (1906).

Forbush Co. v. Bartley, 78 Fed. (2) 805 (C. C. A. 10, 1935).

Hyams v. Calumet & Hecla Min. Co., 221 Fed. 529 (C. C. A. 6, 1915).

International Radio & Telephone Co. v. Atl. Communication Co., 290 Fed. 698 (C. C. A. 2, 1923).

Penn. Canal Co. v. Brown, 235 Fed. 669 (C. C. A. 3, 1916).

Vallery v. Denver & R. G. R. R. Co., 236 Fed. 176 (C. C. A. 8, 1916).

Speaking of the basis for this rule, this Court has held:

"The relation of directors to corporations is of such a fiduciary nature that transactions between boards having common members are regarded as jealously by the law as are personal dealings between a director and his corporation; and where the fairness of such transactions is challenged, the burden is upon those who would maintain them to show their entire fairness; and where a sale is involved, the full adequacy of the consideration. Especially is this true where a common director is dominating in influence or in character. This court has been consistently emphatic in the application of this rule, which, it has declared, is founded in soundest morality, and we now add, in the soundest business policy. *Twin Lick Oil Company v. Marbury,*

91 U. S. 587, 588, 23 L. Ed. 329, 330; *Thomas v. Brownville, Ft. K. & P. R. Co.*, 109 U. S. 522, 27 L. Ed. 1018, 3 Sup. Ct. Rep. 315; *Wardell v. Union P. R. Co.*, 103 U. S. 651, 658, 26 L. Ed. 509, 511; *Corsicanna Nat. Bank v. Johnson*, 251 U. S. 68, 90, 64 L. Ed. 141, 155, 40 Sup. Ct. Rep. 82. * * *" (From the opinion of Mr. Justice Clarke in *Geddes v. Anaconda Copper Min. Co.*, 254 U. S. 590, 599, 65 L. Ed. 425, 432.)

Thus, Standard's entire claim is presumptively fraudulent. Under the foregoing decisions, Standard had the burden of proving the fairness of its dealings with Deep Rock as a condition precedent to the establishment of its claim. *In presenting its claim, however, Standard made no attempt at proving the fairness of the charges against Deep Rock included in the open account.* In the first place, its claim as filed, while it contained many items of debits and credits, was actually only a summary of the thousands of transactions which passed through this open account in the period from 1919 to 1933 (I-51-63, II-437, 544, III-27-53). Moreover, none of the witnesses who testified made any showing that the charges included in the open account were fair, reasonable or proper. Nor was it fully disclosed just what services were rendered for the charges that were made. Such a charge, for example, is the utterly extraordinary and unexplained item shown in the open account under the following heading (III-51):

"Date	Paid to	Nature of Expenditure	Amount
1930 Dec.	H. M. Byllesby & Co. and Byllesby Eng. & Mgt. Corp.	Reimbursement for amounts paid for services and expenses of counsel, accountants and others in re acquisition of property of C. B. Shaffer and E. E. Smathers by Shaffer Oil & Refining Co. in 1919	$139,417.29"

Here is a charge made by Standard in December 1930 for services rendered in 1919 in the acquisition of Deep Rock's capital assets. The least that could be done in connection with charges of that kind, is that a full and satisfactory explanation be made of the reason for the twelve year delay, the nature and value of the services rendered, and that they were in fact proper charges against Deep Rock. *Nevertheless, no explanation of any kind for the making of this extraordinary charge appears in this Record.*

This failure of proof is typical of Standard's presentation of its claim. Standard's support of its claim was based chiefly on the fact that the charges included in the open account appear on the books of both Standard and Deep Rock (II-59-61, 267, 543-7). It is admitted that the entries on Deep Rock's books were directed by Standard's Auditing Department (II-62-5, 69, 188, 49, 606-8, 652-76). It would indeed be surprising if the two sets of books did not agree (II-545-6). In *Mathieson Alkali Works v. Arnold Hoffman & Co.*, 280 Fed. 132 (D. C. R. I., 1922), the court held (133-4):

> "• • • the transactions between the plaintiff and defendant corporations were conducted entirely through the agency of officers acting at the same time for both corporations. If this is the fact there is a strong presumption against their validity, and the burden is upon those who would maintain the transactions to show their entire fairness. *Geddes v. Anaconda Mining Co.*, 254 U. S. 590, 599, 41 Sup. Ct. 209; *Corsicana Nat. Bk. v. Johnson*, 251 U. S. 68, 90, 40 Sup. Ct. 82, 64 L. Ed. 141. If it appears that there was a dual agency, as alleged, this may open up a wide range of inquiry into the fairness of accounts that have been rendered. *A settlement or acceptance of accounts rendered requires independent representation of the party to whom they are rendered.*" (Italics ours.)

Thus, the mere fact that the two sets of books agree is no substitute for the proof of fairness required by the decisions of this Court. Moreover, it is also conceded that there were many large transactions between Deep Rock and Standard and its affiliates that did not clear through the open account and the propriety of which has never been exposed to inquiry (II-74-5, 89, 92, 123, 377). Furthermore, the existence of the many fraudulent transactions brought to light in the course of this hearing, and the admittedly interlocking relationship between Standard and Deep Rock, should have at least required the submission of an impartial and competent audit of all of Standard's dealings with Deep Rock (II-280). *It is admitted, however, that no independent audit has ever been made of the transactions between Deep Rock and Standard and its affiliates* (II-525, 437).

We thus have here a situation where Standard, although undoubtedly having the burden of proving the fairness and propriety of its presumptively fraudulent transactions with Deep Rock, has not even attempted to meet that burden. Its failure to meet that burden of proof is of itself sufficient warrant for the denial of its entire claim within the decisions hereinbefore cited.

In the instant case, however, we have even more than just a mere failure of proof. We have hereinbefore pointed out that, under the uncontroverted proofs, the major portion of the inter-company transactions contained in this account are actually fraudulent and unsustainable. We have seen, among others, some $18,000,000 of such charges resulting from the fraudulent Refining Company transactions, the fraudulent Management Company supervision fees, the illegal and extortionate interest and discount charges, and the illegal dividend withdrawals.

We have prepared in graphic form as Chart 3 a summary of these fraudulent and unsustainable charges that are in-

cluded in this open account. As appears on the next page in Chart 3, there are approximately $20,000,000 of such charges which should be eliminated from the Standard claim. It is unimportant whether the invalidity of these charges results from an affirmative finding of their fraudulent nature or by reason of Standard's failure to overcome the presumption of fraud attaching to all of these transactions. If but one-half of these charges are unsustainable, it nevertheless results in a complete elimination of the net debit balance of approximately $9,300,000 upon which Standard bases its claim.

Whether by reason of the Instrumentality Rule or by elimination of the specific wrongful charges contained in the open account, we submit that the completed and substantially uncontroverted proofs on the merits of the Standard claim disclose beyond question that Standard's claim is invalid and should be denied in its entirety.

C.

THE COMPROMISE ALLOWANCE OF STANDARD'S CLAIM IS UNFAIR AND UNWARRANTED

We have thus far seen that the uncontroverted facts in the instant Record disclose the fraudulent looting by Standard of its completely dominated subsidiary, the Debtor. It is a story of corporate thievery which, we submit, seldom has been equalled in the reported decisions of this Court. Nevertheless, the practical elimination of the public preferred shareholders is justified by respondents as a necessary part of the Debtor's reorganization primarily on the ground that Standard has prior rights as a creditor of the Debtor to the extent of $5,000,000.

We have seen that Standard's claim is based on an open account between Standard and the Debtor, kept under the

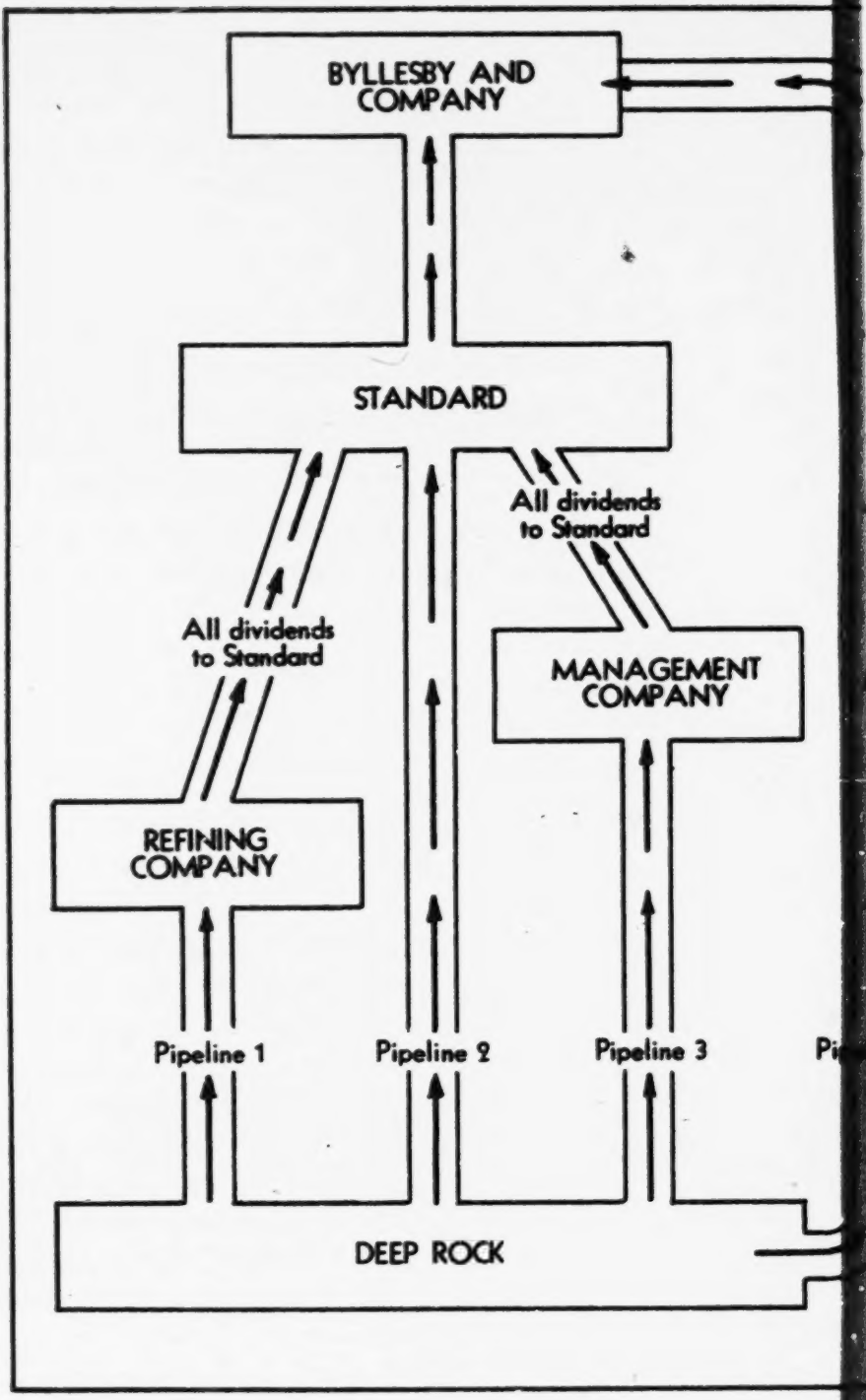
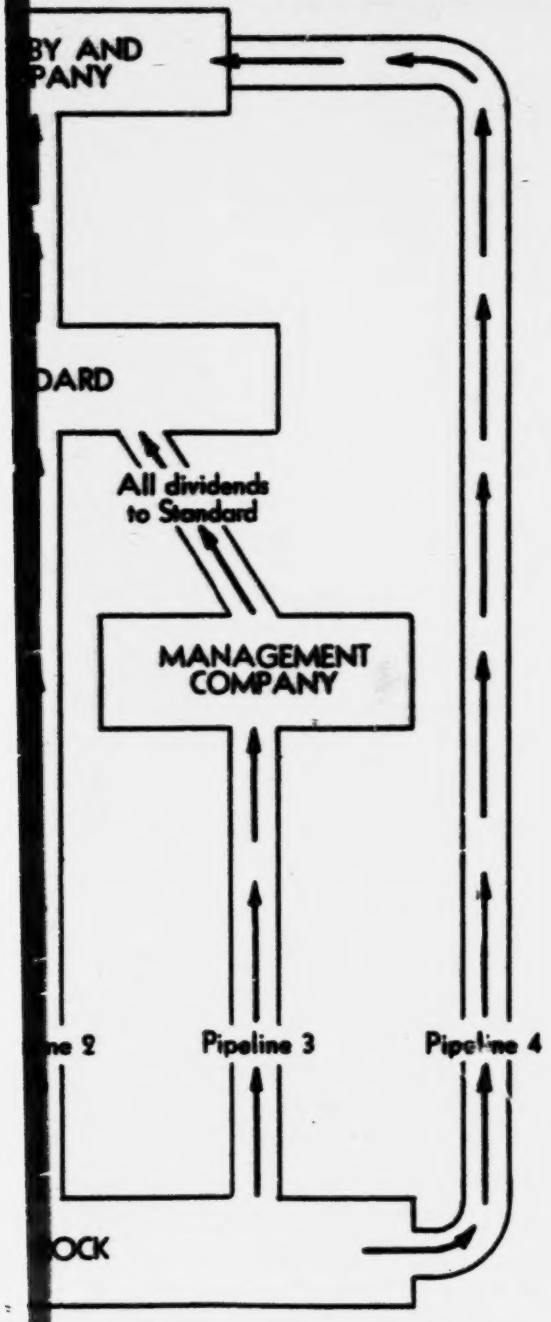

BYLLESBY AND COMPANY
STANDARD
All dividends to Standard
All dividends to Standard
MANAGEMENT COMPANY
REFINING COMPANY
Pipeline 1
Pipeline 2
Pipeline 3
DEEP ROCK

CHART 3

Wrongful Diversion of Deep Rock Assets



	Wrongful charges
Pipeline 1—REFINING COMPANY	
Refining Co. Rentals and Income Tax charges	$ 4,554,565.91
Pipeline 2—STANDARD	
Sundry Expenditures charged to Deep Rock	1,087,569.57
Dividends on Common Stock	102,576.00
Dividends on Common and Preferred Stock (directly to Standard)	4,483,437.00
Assumption by Standard of Deep Rock's open accounts with Standard's subsidiaries	63,350.05
Sale by Standard to Deep Rock of the Home Oil Company stock	175,000.00
Interest and Discounts charged by Standard	6,448,440.69
Pipeline 3—MANAGEMENT COMPANY	
Supervision fees charged to Deep Rock by the Management Company	1,219,034.83
Open account balance of Sundry Charges by Management Co. against Deep Rock, assumed by Standard	230,463.16
Salaries and engineering fees paid directly to the Management Co. by Deep Rock	48,618.93
Pipeline 4—BYLLESBY AND COMPANY	
Commissions for partial extension of the $10,000,000. note issue	312,780.00
Purchase price of 11,000 shares of Utility and Industrial Co. stock sold to Deep Rock by Byllesby and Company	277,475.00
Balance on open account between Byllesby and Co. and Deep Rock, assumed by Standard	752,647.10
The 1922 bill for expenses in 1919 in organizing Deep Rock	142,850.49
Total Wrongful Charges	$19,898,808.73

NOTE: The pipelines show the method of the wrongful diversions of Deep Rock assets and items under the pipeline designations list only the specific items of wrongful charges in Exhibit A of Standard's Claim. These wrongful diversions show a total of $19,898,808.73, which if deducted from Standard's Claim, eliminates Standard's entire claim and leaves Standard indebted to Deep Rock in the amount of $8,011,375.25. (This is after adding to Standard's Claim the Refining Company's debt of $2,544,591.11, thereby reversing the credit entries which Standard ordered in the Refining Company transaction.)

sole direction and control of Standard, and reflecting only its own self-serving dictations throughout the period of its handling of the Debtor. This open account consists of an aggregate of many debit and credit charges, with a net debit balance on which Standard bases its claim. That net debit balance, as we have shown, is entirely eliminated when the fraudulent and unsustainable debit charges are removed from that account. Moreover, we have shown that Standard's abusive handling of the Debtor and its securityholders requires the application of the Instrumentality Rule to deny Standard's claim as a creditor and to relegate its net advancements, if any, to the position of a capital investment in the Debtor.

In reply to our showing of the actual invalidity of the Standard claim, respondents have taken the position that that question is not in issue in this case. Respondents have based their complete avoidance of that issue on their contention that the only issue before the Court is the question of the propriety of the District Court's exercise of its discretionary powers in approving the compromise. In taking that position before this Court, respondents are raising the same smoke screen that they have thus far successfully used both before the District Court and with the majority members of the Circuit Court of Appeals, in avoiding an inquiry into the real merits of the Standard claim.

To appreciate the insincerity of their position, it must be borne in mind that Standard's claim was allowed through a compromise mechanism solely at the behest of respondents and despite petitioners' insistence that the claim be adjudicated on its merits. The basic problem in the instant reorganization was, from the inception of the Debtor's receivership, the question of whether or not Standard had a valid claim as a creditor. Even the Chairman of the Respondent Reorganization Committee admitted this much when he said:

> "When I first got into this situation, I realized that the crux of the Deep Rock is the question of the validity of the Standard claim. It is correct that, depending upon whether or not Standard has a claim, depends the entire form and substance of any plan of reorganization that is to be submitted" (II-425).

Accordingly, the validity of the Standard claim was litigated in a trial on its merits which lasted over one and one-half years and which was finally completed when both sides rested their case on February 13, 1935 (II-241-2). The completed proofs in that trial disclosed, as we have seen, that there was no substantial controversy over the facts and that the issue of the validity of the Standard claim was primarily a question of law. At that time, the completed trial on the merits presented for decision the single question of the validity of the Standard claim. There was no reason whatever why the Standard claim should not then have been fully adjudicated on its merits. This was admitted by the Chairman of the Respondent Reorganization Committee, when he testified on cross-examination:

> "Now at that time (February 13, 1935), I don't know of any reason why the Standard claim should not have been determined on its merits, the hearing terminated and the Standard claim adjudicated" (II-440-1).

Despite that admission, respondents sought to avoid a decision on the validity of the Standard claim by presenting in March, 1935, the so-called first compromise proposal to allow Standard's claim at $5,000,000 (I-102-7). Respondents sought thereby to substitute the new issue of the exercise of discretionary powers in connection with a compromise, in place of the basic issue as to the validity of the Standard claim. This attempt to sidetrack this basic issue was defeated solely by the Taylors, predecessors of petitioners, when the District Court sustained their objections

to the first compromise proposal (I-244-5). At that time, the Honorable District Judge stated in open court his opinion that the entire Standard claim was invalid and unsustainable by reason of the applicability of the Instrumentality Rule of law (II-406-7).

Certainly by that time it was clear that any allowance of Standard's claim at a substantial amount through the medium of a compromise was entirely unwarranted and could only be explained as an attempt to evade a decision on the basic issue of the invalidity of the Standard claim. Respondents, nevertheless, continued their determined effort to evade a decision on the merits of the Standard claim by presenting a second compromise proposal in November, 1936, to allow that claim at the same figure of $5,000,000 (I-296, II-731-4). This second attempt proved successful, despite the best efforts of petitioners to secure an adjudication on the completed proofs on the merits of the Standard claim.

We submit that the District Court's rejection of the first compromise proposal on the ground of the invalidity of the Standard claim was *res adjudicata,* either of the invalidity of the entire Standard claim or at least of the impropriety of a compromise allowance of that claim at $5,000,000.

Adler v. Jones, 109 Fed. 967 (C. C. A. 6, 1901).

Lewith v. Irving Trust Co., 67 Fed. (2) 855 (C. C. A. 2, 1933).

In re Graham & Sons, 252 Fed. 93 (C. C. A. 7, 1918).

In re J. H. Small Shoe Co., 5 Fed. (2) 956 (C. C. 2, 1925).

In the Matter of Youtie, 44 Fed. (2) 56 (C. C. A. 3, 1930).

Ullman, Stern & Krausse v. Coppard, 246 Fed. 124 (C. C. A. 5, 1917).

Union Parlor Furniture Co. v. Weiser, 45 Fed. (2) 711 (C. C. A. 1, 1930).

Wheeling Structural Steel Co. v. Moss, 62 Fed. (2) 37 (C. C. A. 4, 1932).

2 *Freeman, Judgments* (5th Ed.), Sections 670-706.

Nevertheless, the District Judge approved this second compromise proposal for the allowance of Standard's claim at $5,000,000 without any oral or written opinion. Nor did he make any attempt to explain or reconcile that decision with his rejection of the first compromise proposal at the same amount pursuant to his then expressed opinion that the entire claim was invalid.

Respondents' chief justification for their insistence on a compromise of Standard's claim in lieu of an adjudication on the merits, is their contention that a compromise would end the litigation. The insincerity of that contention is shown by the admission of the Chairman of the Respondent Reorganization Committee that at the very time this second compromise proposal was submitted, he already knew that it would not end the litigation in view of petitioners' urgent objections (II-449-450). He testified:

> "• • • I knew that as long as the Taylors litigated the validity of that compromise that we couldn't have a final determination of this litigation (II-449) • • •. I knew after the court's order of September 23, 1935, that the Taylors and Mr. Honigman definitely opposed any such compromise proposal as was then before the court. I anticipated that in presenting the compromise proposal that I am now presenting I would likewise get their opposition.
>
> Q. Now then as long as our opposition was in the situation, there wasn't any ending of litigation? There was merely a continuance of litigation, is not that right? A. It could work out that way, yes sir" (II-449-50).

Respondents thus knew, before submitting this compromise proposal, that it would not end the litigation.

Respondents also knew that neither time nor expense could be saved by the compromise as against an adjudication on the merits of the Standard claim. The proofs on that claim had already been completed. It was then known that any appeal from an approval of the compromise would necessarily bring up the entire record in the trial on the merits of the Standard claim. Respondents also knew that such an appeal would delay consummation of the reorganization just as much as an appeal from a decision on the merits. *Respondents thus knew, before submitting the compromise proposal, that they were saving neither time nor expense by compromising as against an adjudication on the merits of the Standard claim.*

The crowning infidelity of respondents' attempt to hide behind the issue of compromise is that the so-called compromise is actually no compromise at all. To appreciate the effect of this compromise it is necessary to understand the significance of the respondents' appraisal of the Debtor's assets at $17,000,000 which was accepted by the District Court (I-358-61). In a reorganization of the Debtor, it is necessary to allocate some $12,000,000 for principal and interest to the noteholders, leaving only an equity of $5,000,000 to be apportioned between Standard and the public preferred shareholders. Standard procured solely for itself the right to that entire $5,000,000 equity in the Debtor's assets by the allowance of its claim at $5,000,000. The compromise allowance of Standard's claim as a creditor at that amount completely eliminated the preferred shareholders from any right to share in that equity. *Thus Standard gained as complete a victory by the compromise as if its claim had been allowed in full.*

To give Standard the entire equity in the Debtor's assets, with practically nothing to the preferred shareholders, is

actually no compromise at all. It is merely a surrender to Standard of the rights of the preferred shareholders. To accomplish that under the guise of compromise is to defile an honorable principle of business and public morality.

Respondent's contention is true, of course, that the matter of the compromise allowance of a claim is basically a matter of sound discretion of the court. It is clear, however, that such discretion must be exercised within the limits of law and fairness. In *Langnes v. Green*, 282 U. S. 531, 541, 75 L. Ed. 520, 526 (1931), Mr. Justice Sutherland said:

> "The term 'discretion' denotes the absence of a hard and fast rule. *The Styria v. Morgan*, 186 U. S. 1, 9, 46 L. Ed. 1027, 1033, 22 Sup. Ct. 731. When invoked as a guide to judicial action, it means a sound discretion, that is to say, a discretion exercised not arbitrarily or wilfully, but with regard to what is right and equitable under the circumstances and the law, and directed by the reason and conscience of the judge to a just result."

See, too,

Rogers v. Hill, 289 U. S. 582, 77 L. Ed. 1385 (1933).

Fairmount Glass Works v. Cub Fork Coal Co., 287 U. S. 474, 77 L. Ed. 439 (1933).

Meccano v. Wanamaker, 253 U. S. 136, 64 L. Ed. 822 (1920).

In re Nesbitt, 282 Fed. 265 (C. C. A. 2, 1922).

Pettegrew v. Pettegrew, 128 Neb. 783, 260 N. W. 287 (1935).

State v. District Court, 213 Ia. 822, 238 N. W. 290 (1931).

If, as we have contended, and as Circuit Judge Bratton found, the claim of Standard is invalid in its entirety, then no conceivable scope of discretion can warrant the com-

promise allowance of that claim at $5,000,000. If the Standard claim is actually invalid, then its compromise allowance in the instant case is clearly an abuse of discretion. Only by considering the true merits of the Standard claim can a court arrive at a determination of its actual validity or invalidity. Respondents, however, insist that such a consideration is not within the province of this Court. In this contention they were upheld by the majority members of the Circuit Court of Appeals, who refused to pass on the merits of the Standard claim. Circuit Judge Phillips states in his opinion:

> "Clearly whether Standard was entitled to the allowance of its claim on the merits is not the issue here presented" (I-492).

Circuit Judge Williams likewise asserts in his opinion:

> "It is not to be understood that I express any opinion as to whether the Deep Rock Oil Corporation was an instrumentality of the Standard Gas and Electric Company" (I-499).

By its refusal to pass on the validity of the Standard claim, we submit that the Court failed to adjudicate the basic issue of the instant case.

Moreover, despite their refusal to adjudicate the validity of the Standard claim, the majority members of that Court indirectly do adjudicate that Standard has a valid claim of $5,000,000 by approving the compromise allowance at that amount. Such an incongruous result is particularly unwarranted where, as here, the validity of the claim is so seriously open to question. *On the only two occasions when the validity of the Standard claim has judicially been passed on, it has been held that the Standard claim is invalid in its entirety.* The District Judge so held in his opinion stated in open court at the time of the

rejection of the first compromise proposal (II-406-7). Circuit Judge Bratton likewise so held in his dissenting opinion (I-505). It is, we submit, exceedingly unfair that without even taking issue with these holdings that the Standard claim is actually invalid in its entirety, the Circuit Court of Appeals nevertheless approved the compromise allowance of that claim at $5,000,000.

Instead of considering the actual merits of the Standard claim, the majority opinions, and particularly the opinion of Circuit Judge Williams, place great reliance upon their off-the-record evaluations of local counsel, the attorney for the Trustee and the Special Master, both of whom had recommended the first compromise proposal (I-490, 499). The fact is, however, that neither of these attorneys had made any recommendations whatsoever on the second compromise proposal. The instant compromise was never submitted to the Special Master, and the Attorney for the Trustee admitted in open court that neither he nor the Trustee was making any recommendations (II-524). Moreover, no explanation is made in either of the majority opinions as to why the earlier recommendations of those individuals should be given any weight, when the District Judge had already rejected those recommendations at the hearing on the first compromise proposal, in language so strong as to characterize the rejection as one impelled by the District Judge's "conscience" (II-406).

We submit that the circumstances of this case disclose the instant compromise as a faithless attempt to secure for Standard the allowance of a $5,000,000 claim when in fact and law it has no claim whatsoever. From the standpoint of the preferred shareholders, the compromise was clearly contrary to the statutory requirement that it be "for the best interests of the estate" (Section 27 of the Bankruptcy Act, 11 U. S. C. A. Sec. 50). *It is submitted that in no reported case has the compromise allowance of a claim been*

permitted under circumstances comparable to the instant case. In no case has a claim been allowed by compromise where, as here, the following circumstances were present:

(1) Full proofs in a trial on the merits of the claim had already been completed.

(2) The proofs on the claim were substantially undisputed, making the issue of the validity of the claim basically an issue of law.

(3) The claim is not such as appears in the usual course of business, but, on the contrary, involves intercorporate dealings between a parent company and its subsidiary, with debits and credits running over a period of many years supported by nothing more than the self-serving dictations of a single management.

(4) The common directorate of the parent claimant and the Debtor requires, as a matter of law, the application of the rule that the claim is presumptively a fraudulent one. Through the compromise, the claimant sought to avoid its burden of proving the fairness of its self-dictated dealings with the Debtor.

(5) The undisputed facts disclose that the claim is based on a series of fraudulent and unsustainable transactions imposed on the Debtor for the benefit of the parent claimant.

(6) The uncontroverted facts further disclose a situation calling for the application of the Instrumentality Rule of law in denial of the parent company's entire claim as a creditor of its "instrumentality" subsidiary.

(7) A similar compromise had already been rejected under an opinion by the District Court that the entire claim was invalid (II-406-7).

(8) The compromise was clearly contrary to the best interests of a five million dollar class of public preferred shareholders who were being wiped out by the compromise of the Standard claim as effectively as by an adverse adjudication on the merits.

(9) It was known prior to its presentation that the compromise would not end the litigation and that no time or expense would be saved by the compromise as against an adjudication on the merits.

(10) No proofs were submitted in support of the fairness of the compromise and the compromise was submitted and recommended only by Standard, without any submission or recommendation by the Trustee of the Debtor, contrary to the statute and rule governing compromise of claims in Bankruptcy. Section 27 of the Bankruptcy Act, (11 U. S. C. A. Sec. 50) and General Order in Bankruptcy No. 33 (11 U. S. C. A. Sec. 53). See, too, *Utilities Power and Light Corp. v. Irving Trust Co.*, 68 Fed. (2) 359 (C. C. A. 2, 1934); *Petition of Baxter*, 269 Fed. 344 (C. C. A. 6, 1920).

It is respectfully submitted that under all of the foregoing circumstances, no conceivable scope of judicial discretion should warrant the instant compromise allowance of Standard's claim.

D.

THE PLAN OF REORGANIZATION IS UNFAIR BECAUSE IT IS BASED ON AN UNFAIRLY LOW APPRAISAL OF THE DEBTOR'S ASSETS

We have thus far seen that the Plan of Reorganization for the Debtor is predicated upon two basic premises—(1) that Standard has a valid claim as a creditor in the amount of $5,000,000; and (2) that the fair value of the Debtor's assets does not exceed the appraisal of $17,000,000 submitted by respondents. By these two basic assumptions, respondents demonstrate that there is no equity left for the public preferred shareholders, and thereby justify the practical elimination of their investment under the plan of reorganization. The fallacy of the first of these assumptions has been the subject matter of our argument up to this point. We propose here to show that the second of these assumptions is equally fallacious.

There was but one appraisal submitted by the proponents of the Plan, the so-called Trustee's appraisal which was approved by the District Court (I-358-361). By that appraisal, the Debtor's assets are valued at $16,800,000. Of that amount, $7,300,000 represents net current assets consisting mainly of cash, the valuation of which is not in dispute. The Debtor's fixed assets are valued at $9,500,000. That valuation, we submit, is grossly inadequate and was arrived at by an appraisal that was neither fair nor disinterested.

The most serious aspect of the unfairness of that appraisal was its failure to take into account the earnings or earning power of the Debtor. The manner in which this appraisal was prepared is described by Mr. Greis, Trustee of the Debtor, when he testified:

> "In the preparation of this appraisal I took department by department and I subdivided those de-

partments, putting a valuation on each subdivision, and the way I arrived at my total value was by adding up those figures" (II-527).

Not only was this appraisal made by adding up "department by department" but in turn each department was broken down into hundreds of separate units and valued on the basis of cost of reproduction less depreciation to date (II-500, 472-507).

This method of evaluating the Debtor's fixed assets entirely ignored the basic element of the Debtor's going-concern value as indicated by its earnings. This was admitted by the sole expert witness produced by the proponents of the Plan in support of this appraisal. He acknowledged that he had had nothing to do with the making of the appraisal, but was called in after that appraisal was filed in court in order to testify as to the methods used (II-483-4). He testified under cross-examination:

"Q. But the net earning power of the whole picture has not been taken into account, has it?
A. Not by me.
Q. Did they produce any figures to you on which you could take it into account?
A. No, sir.
Q. So that that element, which to a purchaser would be one of the chief elements in purchasing, is not reflected in the appraisal on file here?
A. That is true" (II-504).

The Trustee of the Debtor likewise acknowledged that no consideration had been given to earnings or earning power of the Debtor in the computation of this appraisal (II-528-9). Moreover, the District Judge himself, at the close of the proofs on this appraisal, stated in open court:

"The Court: There is no doubt you have a low appraisement. It is a very conservative appraisement,

because your testimony established you didn't pay any attention to the earning power" (II-566).

Nevertheless, the District Judge approved this appraisal without any written or oral opinion, or any attempt at reconciling the foregoing statement made by him in open court (I-371-2).

The failure to take into account the Debtor's earnings or earning power is particularly unwarranted in view of its actual earning experience and potentialities. The earnings of the Debtor have been very substantial, amounting to over $193,000,000 of gross earnings in the 14 year period of its existence prior to receivership (II-649). Of course, the net result of the Debtor's operations during that period showed considerable losses. We have seen, however, that that result must be attributed to the constant drainage upon its assets through Standard's continual looting as well as through the many millions of dollars paid out in interest and refinancing charges occasioned by the inadequate capital structure which Standard set up. In the three years since receivership, when Standard was deprived of its opportunity for looting, the Debtor has accumulated from earnings over $4,000,000 in cash, as well as millions of dollars in additions and improvements to its fixed assets (II-519, III-132).

The requirement that the earning power of a corporation must be taken into account in any fair valuation of the assets of a going concern has been recognized on every occasion that it has come before the courts. Some of these decisions are:

First National Bank v. Flershem, 290 U. S. 504, 78 L. Ed. 465 (1934).

National Surety Co. v. Coriell, 289 U. S. 426, 77 L. Ed. 1300 (1933).

Ahlenius v. Bunn Humphries, Inc., 358 Ill. 155, 192 N. E. 824 (1934).

Allied Chem. & Dye Corp. v. Steel & Tube Co., 14 Del. Ch. 64, 122 Atl. 142 (1923).

Borg v. International Silver Co., 11 Fed. (2) 147 (C. C. A. 2, 1925).

Doyle Dry Goods Co. v. Lewis, 5 Fed. (2) 918 (C. C. A. 8, 1925).

The failure to take into account the Debtor's earnings and earning power inevitably resulted in an unfairly low appraisal of the Debtor's fixed assets. It was to Standard's interest to arrive at a low valuation of the Debtor's assets in order to justify the elimination of the preferred shareholders from any equity in the Debtor's assets. It is undisputed that this so-called Trustee's appraisal was prepared not by the Trustee, but by the operating heads of the various departments of Deep Rock (II-526, 484). These same employes were originally hired by Standard and were retained by the Trustee in the operation of the Debtor (II-519). Under the plan of reorganization they will again be in Standard's employ (II-463). These same employes had previously submitted appraisals of the Debtor's fixed assets in an amount four times higher than now claimed when it suited Standard's needs in the manipulation of the Debtor's assets and securities (I-43, II-102, 534-5, 297-301, III-103-120, 125). With their primary allegiance to Standard, it is little wonder that they submitted the instant appraisal to again suit Standard's needs, although it was by far the lowest appraisal ever made of the Debtor's fixed assets (III-125, II-102, 534-5) (I-43) (III-103-120) (II-676-9) (III-130) (III-146, II-519, 512-14) (II-781-2, 537-40).

Moreover, the Trustee who lent his name to this appraisal had, as receiver of Deep Rock, already made a

substantially higher appraisal of these same fixed assets (III-146, II-512-14). This former appraisal was first discovered in the course of the cross-examination of the Chairman of the Respondent Reorganization Committee with reference to a letter he had previously sent (II-511-13). Petitioners then learned, for the first time, that the fixed assets which are now appraised by the Trustee at $9,500,000 were, on August 1, 1933, over three years earlier, appraised by the same Trustee at over $13,000,000 (III-146).

The gross discrepancy of the present appraisal is further accentuated by the fact that this self-same Trustee testified that since the time of his 1933 appraisal, the fixed assets of the Debtor have increased in value by approximately $3,000,000 to $4,000,000 (II-519). *If we take this testimony of the Trustee, coupled with his 1933 appraisal, we find that the fixed assets of the Debtor should have a value not of $9,500,000 as he now claims, but instead, a value of over $16,000,000. No attempt was made by the Trustee to explain or justify that gross discrepancy.* Such a discrepancy is not merely unfair. When, under the instant circumstances, the lower appraisal is used to justify the practical elimination of the public preferred shareholders on the ground that there are not sufficient assets to take care of them, it is nothing short of a fraud upon their rights.

The only witness who appraised the fixed assets of the Debtor in the light of its earnings and earning power was the expert witness produced by petitioners (II-551-555). He appraised the fixed assets at $13,600,000 (II-554). That his appraisal was a conservative one, is evidenced by the fact that it was far lower than any appraisal ever made of the Debtor's assets with the single exception of the present Trustee's appraisal. Added to the current assets, that

appraisal results in a total value for the Debtor's fixed and current assets of approximately $21,000,000. On that appraisal, there is sufficient value in the Debtor's assets to pay some $12,000,000 for principal and interest in full to the noteholders, as well as $5,000,000 to Standard, assuming it has a valid claim in that amount, and still leave an equity of approximately $4,000,000 for the preferred shareholders.

For the purpose of ready comparison of the various appraisals of the Debtor's fixed assets which appear in this Record, we have prepared Chart 4, which appears at the next page. *As Chart 4 shows, the present Trustee's appraisal was by far the lowest appraisal ever made of the Debtor's assets and is grossly disproportionate to all former appraisals.* Through the device of an appraisal that is patently unfair and untrustworthy, Standard seeks to finally effectuate its long efforts at destruction of the investment of the public preferred shareholders. We submit that the instant appraisal is unfair and that a fair appraisal of the Debtor's assets would leave no justification for the practical elimination of the preferred shareholders, as provided in the instant Plan of Reorganization.

This Court, through the opinion of Mr. Justice Brandeis, in the case of *National Surety Co. v. Coriell, supra,* reversed the confirmation of a plan of reorganization in a Federal Equity receivership. In so doing, the opinion pointed out that "a trustworthy appraisal" by "a disinterested appraiser" was a necessary prerequisite to a fair plan of reorganization (77 L. Ed. 1305-6). This Court there further pointed out that a fair appraisal must take into account "results of the operation of the business" (77 L. Ed. 1306). These requirements were further stressed by this Court in the subsequent case of *First National Bank v. Flershem, supra,* wherein this Court,

CHART 4

A Comparison of the Various Valuations of the Fixed Assets of Deep Rock, Appearing in this Record

THE VALUATIONS	FIXED ASSETS OF DEEP ROCK
I. "Basis for Appraisal," as of December 31, 1929. (III-125, II-102, 193, 534-5). (Used by Standard in declaring 1930 dividends.)	$37,700,000
II. "Statement of Condition," as of Feb. 28, 1933. (I-43.) (Book values shown at time of receivership and on the same basis as shown in the reports of Deep Rock's condition, published and distributed by Standard.) (II-595-605, III-103-114.)	$37,600,000
III. Riddle valuation, as of December, 1932. (II-676-9.) (Riddle's report to O'Brien, President of Standard and Deep Rock, of the condition of Deep Rock.)	$19,200,000
IV. Trustee's Estimated Reproduction Cost, as of Sept. 1, 1936. (III-130.)	$16,300,000
V. Trustee's Aug. 1, 1933 Appraisal (as modified by his testimony of December 12, 1936, that fixed assets have increased over $3,000,000. since that time.) (III-146, II-519, 512-14.)	$16,200,000
VI. Valuation of fixed assets authorized for depreciation base in Amended Plan, Nov. 9, 1936, as proposed by the Reorganization Committee and approved by the Court. (II-781-2, 537-40.)	$14,400,000
VII. Smith Appraisal, December 12, 1936. (II-554.) (Testimony of only expert who considered earning power of Deep Rock.)	$13,600,000
VIII. Trustee's Final Appraisal of Deep Rock, as of Oct. 31, 1936, approved by the Court. (I-361.) (Based on valuations by Deep Rock employees of individual departments of Deep Rock.)	$9,500,000

after granting certiorari, reversed the decision of the Circuit Court of Appeals entirely by reason of an inadequate appraisal of the assets. In that case, Mr. Justice Brandeis again pointed out the indispensability of an appraisal "by independent experts" which values the assets of a corporation "as an entirety as a going concern" (78 L. Ed. 472, 478).

Particularly in 77-B proceedings, the importance of a fair and disinterested appraisal of the Debtor as a going concern can scarcely be overestimated. See *Jamieson v. Watters*, 91 Fed. (2) 61 (C. C. A. 4, 1937); *Price v. Spokane Silver & Lead Co.*, 97 Fed. (2) 237 (C. C. A. 8, 1938). Reorganization proceedings under Section 77-B are primarily intended to continue the Debtor as a going concern. To value the assets of the Debtor in 77-B proceedings without giving consideration to its earning power as a going concern violates the basic nature of the 77-B Act. It is respectfully submitted that this Court, by its decision in the instant case, should propound the rule that an appraisal in 77-B proceedings must take into account the earnings of the Debtor as a going concern and must comply with the same principles of fairness which this Court has already laid down for equity receiverships. We respectfully submit that the basic requirements for a fair and disinterested appraisal stamp the instant appraisal as unworthy of approval by this Court.

E.

THE OFFER OF THE PLAN AND ITS ACCEPTANCE ARE IN BAD FAITH.

Section 77-B provides, in part:

> "* * * the Judge shall confirm the plan, if satisfied that * * * the offer of the plan and its acceptance are in good faith and have not been made or procured by any means or promises forbidden by this title". (Sec. 77-B (f), 11 U. S. C. A. 207).

It is submitted that in the instant case, neither the offer of the plan nor its acceptance were in good faith. On the contrary, Standard through control of the Debtor and the Respondent Reorganization Committee, has by unfair means procured approval of the instant compromise and Plan of Reorganization. By unfair means, Deep Rock's public preferred shareholders have been deprived of their rightful participation in the Debtor's assets.

Standard controlled the Debtor prior to its receivership and the evidence is uncontradicted that Standard has continued to control the Debtor throughout the reorganization proceedings. Of the present directorate of the Deep Rock Board, 8 out of the 12 directors are Standard officers or directors (II-338, 331). The remaining four are operating officers of Deep Rock who, as we have seen, throughout Deep Rock's history acted with complete servility in the carrying out of Standard's wishes. It is this board of directors which sought the approval of the discredited first plan of reorganization under a petition signed by John J. O'Brien, President of Standard in his capacity as President of Deep Rock (I-68-70). There can be no question under the undisputed facts of this Record that Standard is using the Debtor for its

own ends in the reorganization proceedings just as clearly as it did prior to those proceedings.

The Respondent Reorganization Committee has likewise been created and employed as Standard's instrumentality in the accomplishment of Standard's aim to wipe out the public preferred shareholders. The Reorganization Committee was admittedly organized by Byllesby and Company, the top holding company controlling Standard (II-423-4, 312). Its Chairman is a vice-president of Byllesby and Company, its Secretary is an employe of Byllesby and Company, and its offices are the offices of Byllesby and Company (II-423-4, 465, 717). The remaining personnel of the Committee were all chosen by Byllesby and Company (II-424). The same officers who controlled Standard are also the top officers of Byllesby and Company and as such, are admittedly superior in command to Mr. Shinners, Chairman of the Reorganization Committee (II-422-3).

As we have hereinbefore seen, the basic problem in the instant reorganization was known at the outset to be the question of the validity and extent of the Standard claim (II-425). Thus this Standard controlled Reorganization Committee was faced at the outset with a basic conflict of interest in either protecting the public securityholders by opposing the Standard claim, or protecting Standard by upholding it. In the conflict of loyalties with which this Reorganization Committee was confronted, Deep Rock's public securityholders suffered by the result. Thus at the very outset, Mr. Shinners, Chairman of the Reorganization Committee, found himself in the position where, by his own admission, he knew that his own superiors were guilty of wrongdoing against Deep Rock but he was in no position to call them to account (II-432-4, 462). He testified under cross-examination:

"Q. So that at the middle part of 1933 you had here a situation where you knew these men had made charges that were entirely uncalled for? A. That was my opinion.

Q. That was your opinion? A. Yes, sir.

Q. These men at that time were still your superior officers? A. Yes, sir.

Q. Did you go to them and tell them your opinion at that time? A. Yes, sir.

Q. Did you accuse them of any wrong dealing in the handling of this corporation? A. No, sir.

Q. What did you accuse them of? A. I didn't accuse them at all" (II-434).

Such is the background of the Committee that undertook to reconcile the conflicting interests of Standard and the Debtor's public securityholders.

From the outset, the respondent Committee, instead of opposing the Standard claim or urging upon Standard fair treatment for the public securityholders, undertook to ask for deposits of securities under the now thoroughly discredited first plan of reorganization (II-819-65, I-138-42). That plan of reorganization, as we have seen, provided for practically a total elimination of the preferred shareholders. Its effect was described by the District Judge, when he said:

> "I would just as well say to the (preferred) stockholders, you are wiped out" (II-406).

Thus from its inception the Reorganization Committee urged a plan which, if adopted, would wipe out the preferred shareholders whom it purported to represent.

In order to accomplish adoption of the first Plan of Reorganization, the Reorganization Committee, as we have seen, urged acceptance of the first proposal to compromise the Standard claim at $5,000,000 (II-399-400). It was only by the single-handed effort of the Taylors, predecessors of

petitioners, that that attempt at complete wipe-out of the preferred shareholders was frustrated (I-244-5).

That the Reorganization Committee has at no time taken any steps to oppose the Standard claim is attested to by their own admission (II-426). Instead, we have seen in our consideration of the compromise, that throughout they actively aided Standard in its attempt to evade an adjudication on the merits of its claim. From the outset, the public securityholders were told by the Reorganization Committee that Standard had a justifiable claim of over $7,000,000 (II-824). That statement was repeated even after the District Judge had rejected the first compromise proposal on his expressed opinion that the entire Standard claim was invalid (II-468, 448, 406-7). The representations of the Reorganization Committee that Standard had a valid claim well in excess of the compromise figure were, we submit, clearly unwarranted and in bad faith in view of the facts we have hereinbefore seen. Yet it was in reliance on such representations that the public securityholders deposited their securities with the respondent Committee.

In opposing petitioners' efforts to secure fair treatment for the preferred shareholders, the Reorganization Committee has not hesitated to use every trick and artifice available to such committees. Space does not permit us to detail all of these. We desire merely to point to a few. For example, in one letter from the Reorganization Committee to Deep Rock's preferred shareholders, the securityholders were told that the District Court would pass on the fairness of the plan regardless of the number of securityholders who withdrew from the Reorganization Committee and joined with petitioners (II-682-4). The letter concluded that consequently there was no reason for the securityholders to withdraw their deposits from the Reorganization Committee (II-683-4). That this suggestion

was totally unwarranted, the Chairman of the Reorganization Committee ruefully admitted upon cross-examination:

> "Q. * * * By getting this letter, Intervener's Exhibit 5, securityholders were asked to believe that they will get just as much of a hearing on the fairness of the plan if they joined with the Taylor Committee, as if they stuck with your Committee. A. I think so, yes, sir.
>
> Q. As a matter of fact the order that was entered on the petition of the Committee under date of November 9, 1936, provides that if they do not withdraw from your committee, that by that they approve the plan? A. That is right.
>
> Q. So that by not withdrawing from your Committee these people are in effect saying that they think the plan is fair. A. That is right" (II-458-9).

Thus the securityholders were told that they need not withdraw their securities from the respondent Committee since the court would in any event pass upon the fairness of the plan. They were not told, however, that their very failure to withdraw their securities was an acceptance of the Plan and an acknowledgment of its fairness.

It was in this same letter that the Reorganization Committee informed the securityholders:

> "*The Trustee of Deep Rock and his counsel have approved the new compromise.* The Trustee of Deep Rock and his counsel, both appointees of the court and entirely independent of any connection with Standard, thoroughly investigated all matters relating to the Standard claim and have approved the new compromise thereof after fully considering all contentions asserted by the Taylor Committee" (II-683).

This representation was absolutely false. At the hearing in open court, the Trustee, upon advice of his counsel refused to be examined upon the fairness of the compromise

proposal on the ground that he had nothing to do with it and had "never seen it" (II-522-4). The following colloquy then took place:

> "The Court: You as counsel for the Trustee, have filed no recommendations here on behalf of the Trustee to either accept or reject the compromise?
> Mr. Ramsey (attorney for Trustee): That is right.
> Mr. Honigman: That is definite, is it?
> The Court: Yes.
> Q. (By Mr. Honigman) You agree with that, Mr. Greis (Trustee)? A. Yes, sir" (II-524).

The Reorganization Committee further aided Standard by sponsoring the highly unusual procedure of combining the compromise allowance of the Standard claim with approval of the Plan of Reorganization after admitting that such a procedure was impractical and, we submit, unwarranted under the 77-B Act (II-409-10, I-381-2, 393-5).

In further aiding Standard's aims, the Reorganization Committee accepted the palpably low appraisal of the Debtor's assets, although it knew of the former appraisals which showed a far higher valuation (II-451-3, 462, 511-13). Certainly, the Committee knew, as the evidence in this case discloses, that their appraisal did not take into account the earnings of the Debtor. Yet the pamphlet sent to the securityholders by the Reorganization Committee, containing the Amended Plan, sets forth:

> "As stated in our announcement of the original plan, this Committee gave primary consideration to earning power rather than property values in formulating the original plan. The same considerations have motivated the Committee in formulating the Amended Plan" (II-727).

That representation was a complete falsehood under the undisputed testimony in this case. The appraisal on which

the instant Plan is based, admittedly, as we have seen, gave no consideration to the Debtor's earnings or "earning power" (II-501-4, 528-9, 566).

We submit that the Record in this case leaves no doubt that the Reorganization Committee has throughout aided Standard in the accomplishment of its aim to wipe out Deep Rock's preferred stockholders. Its only end in view has been the protection of the interests of Standard. It has been doubly faithless in the breach of its fiduciary responsibilities to the public securityholders who relied on it.

We have read with a great deal of interest the report of the Securities and Exchange Commission recently filed pursuant to an Act of Congress (Sec. 211 of the Securities Exchange Act of 1934) entitled "Report on the Study and Investigation of the Work, Activities, Personnel and Functions of Protective and Reorganization Committees." That Report formed the basis for many of the amendments to Section 77-B contained in the recently enacted Chandler Act. *We submit there is hardly a single trick that is employed by unscrupulous reorganization committees, as disclosed by that Report, that cannot be found in the facts of the instant case.* In that Report, it appears that in other reorganizations, the activities of Byllesby and Company reorganization committees, including Mr. Shinners, appear by name and often, as prominent actors in reorganization committee activities that are there disclosed to be wrongful and reprehensible (Part I-143-50, 183, 208-9, 245-7, 283-90, 293-6, 360-4, 402-5, 468-9, 496-500, 572-6, 577-85, 614-22, 798-803, Part II-121-160).

We find there an exposition of the very abuses which are attributable to the Respondent Reorganization Committee. We find there, as here, the evils of self-initiated investment banker and management controlled committees, their power to control reorganizations through sole posses-

sion of the lists of securityholders (I-162), their active campaigns to secure deposits with promises of commission to dealers for deposits secured (II-682), their varied forms of misleading and misrepresenting to securityholders, their primary allegiance to the interests of the controlling group at the expense of public securityholders, and their faithlessness in many other respects.

It is therefore particularly appropriate that we quote the conclusions of the Securities and Exchange Commission, as expressed by its one-time Chairman, the Honorable Joseph P. Kennedy (S. E. C. Report, Part II, p. 509):

> "The activities of protective committees constitute one of the most dismal chapters in the annals of American finance. The theory of a protective committee is very simple. A company gets in financial difficulties. A single securityholder cannot act effectively for himself. Hence a committee seeks to secure authority to act for the securityholders. But in practice it has resulted in the most vicious kind of imposition, double-dealing and downright fraud. • • • The first, and by far the more common (type of committee) is the investment banker committee. • • •
>
> The investment banker, except in rare cases, organizes these committees for selfish purposes, and the interests of the securityholders are a secondary consideration at best. • • •
>
> In many instances, the bankers organized a committee for the express purpose of taking command of the reorganization and, by covering up the evidence of their past wrongdoings, insulating themselves against liability. In practically every case, the bankers were motivated by a greedy desire to preserve or secure control, so that they might enjoy the perquisites thereof. This is the equivalent of what we call 'graft' in public life."

We respectfully submit that every charge of wrongdoing there placed upon committees of the type of the instant one, is a warranted judgment of the Reorganization Com-

mittee in this case. The inference of fairness which ordinarily might be drawn from the consents of the majority should not, we submit, be drawn in this case. The preferred shareholders who accepted the Plan and Compromise were either misled by their representative, the Reorganization Committee, as we have already seen, or were prompted by considerations not applicable to the preferred shareholders as a class, as we are about to see.

By far the largest individual holder of preferred shares of Deep Rock, holding 6,000 shares, is Utility and Industrial Corporation, a wholly controlled subsidiary of Bylesby & Company (II-580-4, 715-16). Its acceptance of the Plan was purely at the dictation of its masters, Bylesby and Company and Standard (II-580-1).

The Pitcairn interests, the second largest preferred shareholder, hold 2,350 shares. Prior to the hearing of the Plan, they had joined with petitioners in opposing the Plan (I-33). A few days before the hearing, they suddenly withdrew their powers of attorney from petitioners (I-33-4), and joined with the Reorganization Committee in accepting the Plan (II-872). At the hearing, it developed that their change of position was actuated by reason of their ownership of a large block of Deep Rock notes (I-309). Prior to the hearing, the Reorganization Committee had agreed to double the amount of cash that was to be distributed to noteholders under the Plan as then promulgated (I-302-11). In return for this and other concessions to their position as noteholders, the Pitcairn interests voted their preferred stock in support of the Plan as thus amended (I-33-4, II-463-4).

The Reorganization Committee further represents 969 shares of Deep Rock's preferred stock owned by Standard (II-583-4). *Thus, three of the largest holders of preferred stock, holding a total of 9,319 shares out of the 29,144 shares voting for acceptance, accepted the Plan by reason of spe-*

cial interests not common to the entire class of preferred shareholders (II-579). *Without those acceptances there could not have been a majority acceptance of the Plan.*

The basic rights of minority securityholders to be secure against oppression by the majority is a fundamental principle of law long recognized in receivership cases.

> *Eshleman v. Keenan* (Del. Ch. 1936), 187 Atl. 25.
> *Hamilton-Brown Shoe Co. v. Ben L. Berwald Shoe Co.*, 10 Fed. (2) 275 (C. C. A. 5, 1926).
> *Lake St. El. R. Co. v. Ziegler*, 99 Fed. 114 (C. C. A. 7, 1900).
> *Outwater v. Public Service Corp. of N. J.*, 103 N. J. Eq. 461, 143 Atl. 729 (1928).

In *National Surety Co. v. Coriell*, 289 U. S. 426, 77 L. Ed. 1300 (1933), this Court rejected a plan of reorganization upon complaint by minority securityholders. In so doing, Mr. Justice Brandeis said (437):

> "The creditors who approved of the Plan of Reorganization appeared to be actuated in their recommendations and desires by considerations not applicable to the dissenting creditors."

This Rule is of particular importance in 77-B proceedings where acceptances by the majority are heavily relied upon as evidence of the fairness of a proposed plan of reorganization.

> *Downtown Investment Assn. v. Boston Metropolitan Building*, 81 Fed. (2) 314 (C. C. A. 1, 1936).
> *In re 1775 Broadway Corp.*, 79 Fed. (2) 108 (C. C. A. 2, 1935).

We submit that the instant Record discloses a situation where the offer and the majority acceptances of the Plan were clearly in bad faith. The inference of fairness which ordinarily is drawn from majority acceptances is, we submit, unwarranted under the facts of the instant case.

VII. RELIEF

The instant Plan and Compromise are by their terms made interdependent (I-382, 395, 435, II-733-4). If this Court should find either unfair, it requires a reversal of both. It is the position of petitioners, moreover, that under the facts and circumstances of the instant case, this Court should adjudicate the entire controversy before it. By such an adjudication, we submit, Standard's claim as a creditor should be denied as invalid in its entirety and the so-called Refining Company assets should be adjudged to be the property of the Debtor. The issues as to the validity of the Standard claim and the ownership of the Refining Company assets were fully raised by the pleadings and proofs in the completed trial on the merits of the Standard claim as well as by the instant controversy and appeal (I-51-63, 312-53, 334, 346, 462, 132-3, II-276-290).

The scope of review of an appellate court in bankruptcy cases has long been recognized as a trial *de novo* comparable to an appeal in equity.

> *Houghton v. Burden*, 228 U. S. 161, 57 L. Ed. 780 (1913).
>
> *First National Bank v. Bonner*, 74 Fed. (2) 139 (C. C. A. 10, 1934).
>
> *Chamberlin v. Harrison*, 298 Fed. 926 (C. C. A. 8, 1924).
>
> *Nathanson v. Worcester Bank & Trust Co.*, 73 Fed. (2) 889 (C. C. A. 1, 1934).

Upon such an appeal, appellate courts will completely adjudicate all matters before them even though not passed on in the lower court, as long as those matters were in issue in the court below as well as on appeal.

Denver v. Denver Union Water Co., 246 U. S. 178, 62 L. Ed. 649 (1918).

Elliott v. Toeppner, 187 U. S. 327, 47 L. Ed. 200 (1902).

Houghton v. Burden, 228 U. S. 161, 57 L. Ed. 780 (1913).

Schieber v. Hamre, 10 Fed. (2) 119 (C. C. A. 7, 1926).

In re Goodwine, 298 Fed. 81 (C. C. A. 7, 1924).

Merchants National Bank v. Cole, 149 Fed. 708 (C. C. A. 6, 1907).

We respectfully submit that this Honorable Court should hold the Standard claim invalid and should adjudicate that the Refining Company assets are the property of Deep Rock, free from any claims by Standard.

VIII. CONCLUSION

Under the instant Compromise and Plan of Reorganization, the public preferred shareholders of Deep Rock are being deprived of by far the major part of their $5,000,000 investment. Their loss enures entirely to the benefit of Standard, the parent company, which has throughout been in complete control of the Debtor, looted its assets, sold its securities to the public under misrepresentations and manipulations of value, and now seeks to take the last remaining equity from these same public securityholders by the instant Compromise and Plan of Reorganization. Such treatment for public securityholders should not be countenanced in the absence of a clear showing that it is legally justifiable and inevitable.

Respondents seek to mislead this Court, as they have misled the lower courts, by their insistence that the issue of the invalidity of the Standard claim cannot properly be

considered on the question of the propriety of the compromise allowance of that claim. We submit that this Court should look through respondents' patent attempt to evade an examination into the true merits of the Standard claim. Such an examination will disclose, we submit, that the Standard claim is invalid in its entirety and that the compromise allowance of that claim at $5,000,000 is unwarranted. Aside from the question of the invalidity of the Standard claim and the impropriety of its compromise, we submit that the Debtor's Plan of Reorganization is unfair and unwarranted because it is based on an appraisal of the Debtor's assets that is neither fair nor disinterested.

We respectfully submit that the orders of the lower courts be reversed and that the relief sought by petitioners be granted.

JASON L. HONIGMAN,
Counsel for Petitioners.

A. W. SEMPLINER,
TRAVIS I. MILSTEN,
MILTON J. MILLER,
Of Counsel.